18 Managing Retailing, Wholesaling, and Logistics

In the preceding chapter, we examined marketing intermediaries primarily from the viewpoint of manufacturers that want to build and manage marketing channels. In this chapter, we view these intermediaries—retailers, wholesalers, and logistical organizations—as requiring and forging their own marketing strategies in a rapidly changing world. Intermediaries also strive for marketing excellence and can reap the benefits like any other type of company. Consider the runaway success of Warby Parker.[1]

Started by four Wharton MBA graduates while they were still in school, lifestyle brand Warby Parker is challenging eyewear mammoth Luxottica with a marketing strategy that cleverly combines fashion, value, customer experience, and social responsibility. The company designs its own glasses with a hip if nerdy chic and a fashion ethic that promises, "We will not develop anything that you will be embarrassed to wear in 20 years." With material for frames from a family-owned Italian company, assembly in China, and no middleman, it promises quality comparable to that of well-known designers at a fraction of the cost. Warby Parker eyeglasses start at $95, with free shipping, free exchanges, and free returns. To assess fit, customers can use a virtual try-on tool employing facial recognition technology, have up to five sample pairs shipped to try on in person (free of charge), or visit a retail location. Promoting "eyewear with a purpose," Warby Parker works with a non-profit partner to distribute one pair for every pair sold. To expand reach and engagement beyond its stylish and easy-to-use Web site, the company has launched shops within shops in selected cities, a flagship store in the SoHo area of New York City, and several retail locations across the country. Word of mouth is critical for the brand—50 percent of Web site traffic comes from recommendations by friends and family.

The retail market can be unforgiving. While innovative retailers such as Zappos, Sweden's H&M, Spain's Zara and Mango, and Britain's Topshop have thrived in recent years, others such as former U.S. stalwarts JCPenney, Kohl's, and Kmart have struggled. The more successful use strategic planning, state-of-the-art technology, advanced information systems, and sophisticated marketing tools. They segment their markets, improve their market targeting and positioning, and connect with their customers through memorable experiences, relevant and timely information, and of course the right products and services. In this chapter, we consider marketing excellence in retailing, wholesaling, and logistics.

Retailing

Retailing includes all the activities in selling goods or services directly to final consumers for personal, nonbusiness use. A **retailer** or **retail store** is any business enterprise whose sales volume comes primarily from retailing.

Any organization selling to final consumers—whether it is a manufacturer, wholesaler, or retailer—is doing retailing. It doesn't matter *how* the goods or services are sold (in person, by mail, by telephone, by vending machine, or online) or *where* (in a store, on the street, or in the consumer's home).

Retailing is a fast-moving, challenging industry. Consider the plight of Sears.[2]

SEARS Sears is a classic U.S. company. It was one of the first to sell goods through a mail-order catalog, and for more than 100 years, it was one of the strongest department store brands, associated with high-quality merchandise and responsive customer service. However, in the early 2000s, the company began facing financial difficulties, and to keep its earnings stable, it started aggressively selling assets and cutting costs. Customers began complaining about inattentive sales associates, disorganized sales racks, and stores in disrepair. Sears was spending only $2 to $3 per square foot in annual maintenance and repair of its stores, far less than the $6 to $8 per square foot spent by competitors Target and Walmart. "[T]hey weren't keeping [their] promise. Consumers are pretty sophisticated, and they walked into these stores and it was the same old place . . . without the freshness, the excitement or the interactivity of the experience." According to the ACS index of customer satisfaction, in 2012, Sears ranked 10th among 11 Department and Discount Stores. Given that same-store sales have declined for so many years, many feel Sears' disillusioned customers may not be coming back.

At the same time, there are many retailing success stories. "Marketing Memo: Innovative Retail Organizations" highlights four examples of innovative retail organizations that have experienced market success in recent years. After reviewing the different types of retailers and some important characteristics of the modern retail marketing environment, we examine in detail the marketing decisions retailers make.

TYPES OF RETAILERS

Consumers today can shop for goods and services at store retailers, nonstore retailers, and retail organizations.

STORE RETAILERS Perhaps the best-known type of store retailer is the department store. Japanese department stores such as Takashimaya and Mitsukoshi attract millions of shoppers each year and feature art galleries, restaurants, cooking classes, fitness clubs, and children's playgrounds. The most important types of major store retailers are summarized in Table 18.1.

Different formats of store retailers will have different competitive and price dynamics. Discount stores, for example, historically have competed much more directly with each other than with other formats, though that is

Sears has struggled to stay competitive in the dynamic, constantly changing world of retail.

Source: © Helen Sessions/Alamy

marketing memo — Innovative Retail Organizations

GameStop. Video game and entertainment software retailer GameStop has more than 6,600 convenient locations in malls and shopping strips all over the United States, staffed by hard-core gamers who like to connect with customers. The company boasts a trade-in policy that gives credit for an old game exchanged for a new one. To keep track of the activities of its 25 million customers, it also has a successful data-driven loyalty program, PowerUp Rewards, which offers reward points and allows members to manage their gaming interests with the online Game Library to showcase games members have had in the past, that they currently have, and that they wish they had.

Dick's Sporting Goods. Dick's Sporting Goods has grown from a single bait-and-tackle store in Binghamton, New York, into the largest U.S.-based full-line sporting goods retailer, with approximately 574 stores in 44 states. Part of its success springs from the interactive features of its stores. Customers can test golf clubs in indoor ranges, sample shoes on its footwear track, and shoot bows in its archery range. With an advertising tag line of "Every Season Starts at Dick's," the retailer is also emphasizing the fundamental goal of sports achievement and improvement to establish a stronger emotional connection with customers.

Lumber Liquidators. Lumber Liquidators is the largest hardwood flooring specialty retailer in the United States, with more than 345 locations. The company buys excess wood directly from lumber mills at a discount and stocks almost 350 kinds of flooring, about the same as Lowe's and Home Depot. It sells at lower prices because it keeps operating costs down by cutting out the middlemen and locating stores in inexpensive locations. Lumber Liquidators also knows a lot about its customers, such as the fact that shoppers who request product samples have a 30 percent likelihood of buying within a month and that most tend to renovate one room at a time, not the entire home at once.

Net-a-Porter. London-based Net-a-Porter is an online luxury clothing and accessories retailer whose Web site combines the style of an fashion magazine with the thrill of a chic boutique. Seen by its loyal customers as an authoritative fashion voice, the company publishes its interactive magazine weekly and stocks more than 300 international brands, including Jimmy Choo, Alexander McQueen, Stella McCartney, Givenchy, and Marc Jacobs, as well as many up-and-comers. It ships to 170 countries and offers same-day delivery in London and Manhattan; the average order is $250. A new site, Mr. Porter, targets men.

Sources: *GameStop*: Steve Peterson, "GameStop Sees Targeted Marketing on the Rise," www.thealistdaily.com, September 26, 2013; Jeanine Poggi, "GameStop Revamps Business to Ensure Success in a Digital Future," *Advertising Age*, April 9, 2012; Chris Daniels, "GameStop CMO Sees CRM as Key," *Direct Marketing News*, October 2011; Devin Leonard, "GameStop Racks Up the Points," *Fortune*, June 9, 2008, pp. 109–22; *Dick's Sporting Goods*: "Brand Genius: Lauren Hobart, Chief Marketing Officer, Dick's Sporting Goods," *Adweek*, September 23, 2013; Matt Townsend, "Dick's Channels 'Rudy' in New Branding Strategy," www.bloomberg.com, March 1, 2012; "Dick's Sporting Goods Details Growth Strategy to Reach $10 Billion in Sales and 10.5% Operating Margin by the End of Fiscal 2017," *PR Newswire*, August 3, 2013; *Lumber Liquidators*: Mark Heschmeyer, "Lumber Liquidators Planning to Spruce Up Retail Image, www.costar.com, January 30, 2013; Marilyn Much, "Lumber Liquidators' New CEO Helps Drive Sales Surge," *Investor's Business Daily*, May 17, 2012; Helen Coster, "Hardwood Hero," *Forbes*, November 30, 2009, pp. 60–62; *Net-a-Porter*: David Moth, "How Net-a-Porter Plans to Build on Its Mobile Success in 2013," www.econsultancy.com, March 18, 2013; Christina Binkley, "Finding an Audience for Edgy Runway Styles," *Wall Street Journal*, March 28, 2012; Paul Sonne, "Richemont to Buy Net-a-Porter," *Wall Street Journal*, April 2, 2010; John Brodie, "The Amazon of Fashion," *Fortune*, September 14, 2009, pp. 86–95.

changing, as we'll see below.[3] Retailers also meet widely different consumer preferences for service levels and specific services. Specifically, they position themselves as offering one of four levels of service:

1. ***Self-service***—Self-service is the cornerstone of all discount operations. Many customers are willing to carry out their own "locate-compare-select" process to save money.
2. ***Self-selection***—Customers find their own goods, though they can ask for assistance.
3. ***Limited service***—These retailers carry more shopping goods and services such as credit and merchandise-return privileges. Customers need more information and assistance.
4. ***Full service***—Salespeople are ready to assist in every phase of the "locate-compare-select" process. Customers who like to be waited on prefer this type of store. The high staffing cost and many services, along with the higher proportion of specialty goods and slower-moving items, result in high-cost retailing.

NONSTORE RETAILING Although the overwhelming bulk of goods and services is sold through stores, *nonstore retailing* has been growing much faster than store retailing, especially given e-commerce and m-commerce

TABLE 18.1	Major Types of Store Retailers
Specialty store: Narrow product line. The Limited, The Body Shop.	
Department store: Several product lines. JCPenney, Bloomingdale's.	
Supermarket: Large, low-cost, low-margin, high-volume, self-service store designed to meet total needs for food and household products. Kroger, Safeway.	
Convenience store: Small store in residential area, often open 24/7, limited line of high-turnover convenience products plus takeout. 7-Eleven, Circle K.	
Drug store: Prescription and pharmacies, health and beauty aids, other personal care, small durable, miscellaneous items. CVS, Walgreens.	
Discount store: Standard or specialty merchandise; low-price, low-margin, high-volume stores. Walmart, Kmart.	
Extreme value or hard-discount store: A more restricted merchandise mix than discount stores but at even lower prices. Aldi, Lidl, Dollar General, Family Dollar.	
Off-price retailer: Leftover goods, overruns, irregular merchandise sold at less than retail. Factory outlets; independent off-price retailers such as TJ Maxx; warehouse clubs such as Costco.	
Superstore: Huge selling space, routinely purchased food and household items, plus services (laundry, shoe repair, dry cleaning, check cashing). Category killer (deep assortment in one category) such as Staples; combination store such as Jewel-Osco; hypermarket (huge stores that combine supermarket, discount, and warehouse retailing) such as Carrefour in France.	
Catalog showroom: Broad selection of high-markup, fast-moving, brand-name goods sold by catalog at a discount. Customers pick up merchandise at the store. Inside Edge Ski and Bike.	

as Chapter 17 outlined. Nonstore retailing falls into four major categories: direct marketing (which includes telemarketing and online selling), direct selling, automatic vending, and buying services:

1. ***Direct marketing*** has roots in direct-mail and catalog marketing (Lands' End, L.L.Bean); it includes *telemarketing* (1-800-FLOWERS), *television direct-response marketing* (HSN, QVC), and *online shopping* (Amazon.com, Autobytel.com). People are ordering a greater variety of goods and services from a wider range of Web sites. In the United States, online sales were estimated to be $225 billion in 2012, approaching 6 percent of total retail sales.[4]
2. ***Direct selling,*** also called *multilevel selling* and *network marketing*, is a multibillion-dollar industry, with companies selling door to door or through at-home sales parties. Well-known in such one-to-one selling are Avon, Electrolux, and Southwestern Company of Nashville (Bibles). Tupperware and Mary Kay Cosmetics are sold one-to-many: A salesperson goes to the home of a host who has invited friends; the salesperson demonstrates the products and takes orders. Pioneered by Amway, the multilevel (network) marketing sales system works by recruiting independent businesspeople who act as distributors. The distributor's compensation includes a percentage of sales made by those he or she recruits as well as earnings on his or her own direct sales to customers. These direct-selling firms, now finding fewer consumers at home, are developing multi-distribution strategies.
3. ***Automatic vending*** offers a variety of merchandise, including impulse goods such as soft drinks, coffee, candy, newspapers, magazines, and other products such as hosiery, cosmetics, hot food, and paperbacks. Vending machines are found in factories, offices, large retail stores, gasoline stations, hotels, restaurants, and many other places. They offer 24-hour selling, self-service, and merchandise that is stocked to be fresh. With more than 5 million units, Japan has the highest per-capita coverage of vending machines in the world. You can buy everything from fresh eggs to pet rhinoceros beetles. Coca-Cola has close to 1 million machines there and annual vending sales of $50 billion—twice its U.S. figures.[5]
4. ***Buying service*** is a storeless retailer serving a specific clientele—usually employees of large organizations—who are entitled to buy from a list of retailers that have agreed to give discounts in return for membership.

Without question, online nonstore retailing has been exploding and is taking many different forms. Consider the success of flash-sales Web sites such as Gilt.[6]

GILT During the recent recession, many designer brands found themselves with excess inventory they badly needed to move. Third-party "flash-sales" sites, offering deep discounts for luxury products and other goods for only a short period of time each day, allowed them to do so in a controlled manner less likely to hurt their brands. Modeled in part after France's flash-sales pioneer Vente-Privée, Gilt was launched in November 2007 to sell fashionable women's clothing from top designer labels for up to 60 percent off, but on a limited-time basis and only to those who joined the online site. Members were alerted of deals and their deadlines via e-mails that conveyed a sense of immediacy and urgency. Adding luxury brands such as Theory and Louis Vuitton, the firm grew to more than 8 million members and an estimated value of $1 billion. As the recession wound down, however, Gilt found itself challenged by dwindling inventory, growing competition from other sites, and its own aggressive expansion strategy, which included men's clothes, kids' products, home products, travel packages, and food. The company responded by focusing more on its core strength in women's fashion and developing tighter relationships with customers via personalized e-mails to announce its sales.

Source: © VisualJapan/Alamy

Vending machines can be found almost anywhere in Japan, selling almost any kind of merchandise, including umbrellas.

CORPORATE RETAILING AND FRANCHISING Although many retail stores are independently owned, an increasing number are part of a **corporate retailing** organization. These organizations achieve economies of scale, greater purchasing power, wider brand recognition, and better-trained employees than independent stores can usually gain alone. The major types of corporate retailing—corporate chain stores, voluntary chains, retailer and consumer cooperatives, franchises, and merchandising conglomerates—are described in Table 18.2.

Franchise businesses such as Hampton, Jiffy-Lube, Subway, Supercuts, 7-Eleven, and many others account for more than 10 percent of businesses with paid employees in the 295 industries for which franchising data are collected by the U.S. Census Bureau.[7]

TABLE 18.2	Major Types of Corporate Retail Organizations
Corporate chain store: Two or more outlets owned and controlled, employing central buying and merchandising, and selling similar lines of merchandise. Gap, Pottery Barn.	
Voluntary chain: A wholesaler-sponsored group of independent retailers engaged in bulk buying and common merchandising. Independent Grocers Alliance (IGA).	
Retailer cooperative: Independent retailers using a central buying organization and joint promotion efforts. Unified Grocers, ACE Hardware.	
Consumer cooperative: A retail firm owned by its customers. Members contribute money to open their own store, vote on its policies, elect a group to manage it, and receive dividends. Local cooperative grocery stores can be found in many markets.	
Franchise organization: Contractual association between a franchisor and franchisees, popular in a number of product and service areas. Dunkin' Donuts, Marriott, H&R Block, and The UPS Store.	
Merchandising conglomerate: A corporation that combines several diversified retailing lines and forms under central ownership, with some integration of distribution and management. Federated Department Stores renamed itself after one of its best-known retailers, Macy's, but also owns other retailers such as Bloomingdale's.	

In a franchising system, individual *franchisees* are a tightly knit group of enterprises whose systematic operations are planned, directed, and controlled by the operation's innovator, called a *franchisor*. Franchises are distinguished by three characteristics:

1. The franchisor owns a trade or service mark and licenses it to franchisees in return for royalty payments.
2. The franchisee pays for the right to be part of the system. Start-up costs include rental and lease equipment and fixtures and usually a regular license fee. McDonald's franchisees typically invest about $1.5 million in total start-up costs and fees. The franchisee then pays McDonald's a certain percentage of sales plus a monthly rent.[8]
3. The franchisor provides its franchisees with a system for doing business. McDonald's requires franchisees to attend "Hamburger University" in Oak Brook, Illinois, for two weeks to learn how to manage the business. Franchisees must follow certain procedures in buying materials.[9]

Franchising benefits both parties. Franchisors gain the motivation and hard work of employees who are entrepreneurs rather than "hired hands," the franchisees' familiarity with local communities and conditions, and the enormous purchasing power of being a franchisor. Franchisees benefit from buying into a business with a well-known and accepted brand name. They find it easier to borrow money for their business from financial institutions, and they receive support in areas ranging from marketing and advertising to site selection and staffing.

Franchisees do walk a fine line between independence and loyalty to the franchisor. Some franchisors are giving their franchisees freedom to run their own operations, from personalizing store names to adjusting offerings and price. Great Harvest Bread believes in a "freedom franchise" approach that encourages its franchisee bakers to create new items for their store menus and to share with other franchisees if they are successful.[10]

THE MODERN RETAIL MARKETING ENVIRONMENT

The retail marketing environment is dramatically different today from what it was just a decade or so ago. Here we focus on two areas that have seen enormous change: competitive retail market structure and the role of technology.

COMPETITIVE RETAIL MARKET STRUCTURE The retail market is very dynamic, and a number of new types of competitors and competition have emerged in recent years. Here are five important developments (see Table 18.3 for a summary).

- ***New Retail Forms and Combinations.*** To better satisfy customers' need for convenience, a variety of new retail forms have emerged. Bookstores feature coffee shops. Gas stations include food stores. Loblaw's Supermarkets have fitness clubs. Shopping malls and bus and train stations have peddlers' carts in their aisles. Retailers are also experimenting with "pop-up" stores that let them promote brands to seasonal shoppers for a few weeks in busy areas. Pop-up stores are designed to create buzz often through interactive experiences. Internet companies such as Amazon.com and Google use pop-up stores as an easy way to establish a physical presence during holiday shopping seasons.[11]
- ***Growth of Giant Retailers.*** Through their superior information systems, logistical systems, and buying power, giant retailers such as Walmart are able to deliver good service and immense volumes of product to masses of consumers at appealing prices. They are crowding out smaller manufacturers that cannot deliver enough quantity and often dictate to the most powerful ones what to make, how to price and promote it, when and how to ship, and even how to improve production and management. Without these accounts, manufacturers would lose 10 percent to 30 percent of the market.

  Some giant retailers are *category killers* that concentrate on one product category, such as pet food (PETCO), home improvement (Home Depot), or office supplies (Staples). Others are *supercenters* that combine grocery items with a huge selection of nonfood merchandise (Walmart). With their broad product assortments, reasonable prices, and convenient service, category killers wiped out many smaller specialty

TABLE 18.3 Recent Retail Developments

- New Retail Forms and Combinations
- Growth of Giant Retailers
- Growth of Intertype Competition
- Emergence of Fast Retailing
- Decline of Middle-Market Retailers

Source: © Daily Mail/Rex/Alamy

Many firms set up temporary pop-up stores to create special shopping experiences, especially at Christmas.

retailers. The rise of Amazon.com and other online retailers has nullified their advantages, however, and some category killers such as Borders, Circuit City, and Tweeter have even gone out of business.[12]

- ***Growth of Intertype Competition.*** One consequence of the growth of the supercenters is that department stores can't worry just about other department stores—discount chains such as Walmart and Tesco are expanding into product areas such as clothing, health, beauty, and electrical appliances.[13] Supermarkets also have to worry about these supercenters. Grocery products accounted for 56 percent of Walmart's U.S. sales in 2012, up from 41 percent just six years ago. The reality is that different types of stores can all compete for the same consumers by carrying the same type of merchandise.
- ***Emergence of Fast Retailing.*** An important trend in fashion retailing in particular, but with broader implications, is the emergence of fast retailing. Here retailers develop completely different supply chain and distribution systems to allow them to offer consumers constantly changing product choices. Fast retailing requires thoughtful decisions in a number of areas, including new product development, sourcing, manufacturing, inventory management, and selling practices. As Chapter 12 described, consumers have been attracted to fast-fashion retailers such as H&M, Zara, Uniqlo, Top Shop, and Forever 21 because of the novelty, value, and fashion sense of their offerings and have made them successful. Critics, however, pan fast fashion for its planned obsolescence and the resulting disposability and waste.[14]
- ***Decline of Middle-Market Retailers.*** We can characterize the retail market today as hourglass or dog-bone shaped: Growth seems to be centered at the top (with luxury offerings from retailers such as Tiffany and Neiman Marcus) and at the bottom (with discount pricing from retailers such as Walmart and Dollar General). As discount retailers improve their quality and image, consumers have been willing to trade down. Target offers Phillip Lim, Jason Wu, and Missoni designs, and Kmart sells an extensive line of Joe Boxer underwear and sleepwear. At the other end of the spectrum, Coach converted 40 of its nearly 300 stores to a more upscale format that offers higher-priced bags and concierge services. Opportunities are scarcer in the middle, where once-successful retailers like JCPenney, Kohl's, Sears, CompUSA, RadioShack, and Montgomery Ward have struggled or even gone out of business. Supermarket chains like Supervalu and Safeway have found themselves caught in the middle between the affluent appeal of chains like Whole Foods and the discount appeal of Aldi and Walmart. Compounding problems is the plight of the middle class—the 40 percent of U.S. consumers with annual incomes between $50,000 and $140,000—who have seen their buying power shrink due to slumping housing prices and stagnating incomes.[15]

ROLE OF TECHNOLOGY Technology is profoundly affecting the way retailers conduct virtually every facet of their business. Almost all now use technology to produce forecasts, control inventory costs, and order from suppliers, reducing the need to discount and run sales to clear out languishing products.

Technology is also directly affecting the consumer shopping experience inside the store. Electronic shelf labeling allows retailers to change price levels instantaneously at need.[16] In-store programming on plasma TVs can run continual demonstrations or promotional messages. Retailers are experimenting with virtual shopping screens, audio/video presentations, and QR code integration.

For flagship stores in Taipei, Hong Kong, London, and Chicago, Burberry made "virtual rain" with a 360° film, as part of its digital "Burberry World Live" program showcasing its rain gear. The UK's Marks & Spencer installed marketing insight

The Growth of Shopper Marketing

Buoyed by research suggesting that as many as 70 percent to 80 percent of purchase decisions are made inside the store, firms are increasingly recognizing the importance of influencing consumers at the point of purchase. **Shopper marketing** is the way manufacturers and retailers use stocking, displays, and promotions to affect consumers actively shopping for a product.

Where and how a product is displayed and sold can have a significant effect on sales. A strong proponent of shopper marketing, Procter & Gamble calls the store encounter the "first moment of truth" (product use and consumption are the second). P&G observed the power of displays in a Walmart project designed to boost sales of premium diapers such as Pampers. By creating the first baby center in which infant products—previously spread across the store—were united in a single aisle, the new shelf layout encouraged parents to linger longer and spend more money, increasing Pampers sales. Another successful promotion, this one for P&G's Cover Girl cosmetics brand, tapped into a fashion trend for a "smoky eye" look by developing kits for Walmart and connecting with potential customers on Facebook with instructions, blogs, and a photo gallery.

Retailers are also using technology to influence customers as they shop. Some supermarkets are employing mobile phone apps or "smart shopping carts" that help customers locate items in the store, find out about sales and special offers, and pay more easily. One academic research study found that real-time spending feedback from a smart shopping cart stimulated budget shoppers to spend more (by buying more national brands) but led non-budget shoppers to spend less (by replacing national brands with store brands).

Kraft Foods spinoff Mondelēz uses "smart shelf" technology by putting sensors on shelves near check-out that can detect the age and sex of a consumer and, by virtue of advanced analytics, target them with ads and promotions for a likely snack candidate on a video screen.[18]

Technology is also playing a crucial research role in the design of shopper marketing programs. Some retailers outfit their aisles with sensors or use video from security cameras or other means to monitor shoppers' movements. Others use infrared goggles or wearable video cameras to record what test customers actually see. One finding was that many shoppers ignored products at eye level—the optimal location was between waist and chest level.

Other academic research found that unplanned purchases increased the more a product is touched, the longer a purchase is considered, the closer a customer is to the shelf, the fewer the shelf displays in sight, and the more quickly shoppers can reference external information. To capitalize on these findings, researchers recommend that retailers put Quick Response (QR) codes next to products to be scanned with smart phones. Even the simple act of touching a product on a tablet screen has been shown in research to increase purchase intent.

Sources: Megan Woolhouse, "Tablets Facilitate Impulse Shopping for Many," *Boston Globe*, December 18, 2013; Elizabeth Dwoskin and Greg Bensinger, "Tracking Technology Sheds Light on Shopper Habits," *Wall Street Journal*, December 9, 2013; S. Adam Brasel and Jim Gips, "Tablets, Touchscreens, and Touchpads: How Varying Touch Interfaces Trigger Psychological Ownership and Endowment" *Journal of Consumer Psychology* 24 (April 2014), pp. 226–33; Koert van Ittersum, Brian Wansink, Joost M. E. Pennings, and Daniel Sheehan, "Smart Shopping Carts: How Real-Time Feedback Influences Spending," *Journal of Marketing* 77 (November 2013), pp. 21–36; Barry Silverstein, "Will Mondelez's 'Smart Shelves' Change Retail or Just Add to Privacy Woes," www.brandchannel.com, October 13, 2013; Noreen O'Leary, "Shopper Marketing Goes Mainstream," *Adweek*, May 20, 2013, p. 19; Yanliu Huang, Sam K. Hui, J. Jeffrey Inman, and Jacob A. Suher, "Capturing the 'First Moment of Truth': Understanding Point-of-Purchase Drivers of Unplanned Consideration and Purchase," MSI Report 12-101, www.msi.org, 2012; Pat Lenius, "P&G Leverages Facebook to Enhance Promotions in Walmart," www.cpgmatters.com, November 2011; Venkatesh Shankar, "Shopper Marketing: Current Insights, Emerging Trends, and Future Directions," *MSI Relevant Knowledge Series Book,* www.msi.org, 2011; Anthony Dukes and Yunchuan Liu, "In-Store Media and Distribution Channel Coordination," *Marketing Science* 29 (January–February 2010), pp. 94–107; Richard Westlund, "Bringing Brands to Life: The Power of In-Store Marketing," Special Advertising Supplement to *Adweek*, January 2010; Pierre Chandon, J. Wesley Hutchinson, Eric T. Bradlow, and Scott H. Young, "Does In-Store Marketing Work? Effects of the Number and Position of Shelf Facings on Brand Attention and Evaluation at the Point of Purchase," *Journal of Marketing Research* 73 (November 2009), pp. 1–17; Michael C. Bellas, "Shopper Marketing's Instant Impact," *Beverage World*, November 2007, p. 18; Michael Freedman, "The Eyes Have It," *Forbes*, September 4, 2006, p. 70.

Source: ASSOCIATED PRESS

Smart shopping carts are just one of the technological innovations transforming supermarkets.

virtual mirrors in some of its stores so that, just as on its Web site, customers can see what an eye shadow or lipstick would look like for them without having to physically put it on.[17]

After encountering problems measuring store traffic in the aisles—GPS on shopping carts didn't work because consumers tended to abandon their carts, and thermal imaging couldn't tell the difference between babies and turkeys—bidirectional infrared sensors sitting on store shelves have proven successful. "Marketing Insight: The Growth of Shopper Marketing" describes the important role technology is taking in the aisles.

Retailers are also developing fully integrated digital communication strategies with well-designed Web sites, e-mails, search strategies, and social media campaigns. Social media are especially important for retailers during the holiday season when shoppers are seeking information and sharing successes. For the 2013 holiday season, Toys "R" Us focused on YouTube; Sears used Instagram and hosted holiday parties on Twitter; Target used Pinterest as well as six or seven other social media options.[19] Beyond the holidays, many retailers are linking to customer photos supporting their brands on Instagram, Pinterest, and other sites to create social engagement.[20]

MARKETING DECISIONS

With this new retail environment as a backdrop, we now examine retailers' marketing decisions in some key areas: target market, channels, product assortment, procurement, prices, services, store atmosphere, store activities and experiences, communications, and location. We discuss private labels in the next section.

TARGET MARKET Until it defines and profiles the target market, the retailer cannot make consistent decisions about product assortment, store decor, advertising messages and media, price, and service levels. Whole Foods has succeeded by offering a unique shopping experience to a customer base interested in organic and natural foods.[21]

WHOLE FOODS MARKET In 284 stores in North America and the United Kingdom, Whole Foods creates celebrations of food. Its markets are bright and well staffed, and food displays are colorful, bountiful, and seductive. Whole Foods is the largest U.S. organic and natural foods grocer, offering more than 2,400 items in four lines of private-label products that add up to 11 percent of sales: the premium Whole Foods Market, Whole Kitchen, and Whole Market lines and the low-priced 365 Everyday Value line. Whole Foods also offers lots of information about its food. If you want to know, for instance, whether the chicken in the display case lived a happy, free-roaming life, you can get a 16-page booklet and an invitation to visit the farm in Pennsylvania where it was raised. For other help, you have only to ask a knowledgeable and easy-to-find employee. A typical Whole Foods has more than 200 employees, almost twice as many as Safeway. The company works hard to create an inviting store atmosphere with prices scrawled in chalk, cardboard boxes and ice everywhere, and other creative display touches to make the shopper feel at home. Its approach is working, especially for consumers who view organic and artisanal food as an affordable luxury. From 1991 to 2009, sales grew at a 28 percent compounded annual growth rate (CAGR). Although the recession hit the retailer hard, it did emerge with more double-digit growth.

Whole Foods selects merchandise and creates a homey in-store atmosphere to appeal to organic and natural foods lovers.

Source: Courtesy of Whole Foods Market. "Whole Foods Market" is a registered trademark of Whole Foods Market IP, L.P.

Mistakes in choosing target markets can be costly. When historically mass-market jeweler Zales decided to chase upscale customers, it replaced one-third of its merchandise, dropping inexpensive, low-quality diamond jewelry for high-margin, fashionable 14-karat gold and silver pieces and shifting its ad campaign in the process. The move was a disaster. Zales lost many of its traditional customers without winning over the new customers it hoped to attract.[22]

To better hit their targets, retailers are slicing the market into ever-finer segments and introducing new lines of stores to exploit niche markets with more relevant offerings: Gymboree launched Janie and Jack, selling apparel and gifts for babies and toddlers; Hot Topic introduced Torrid, selling fashions for plus-sized teen girls; and Limited Brand's Tween Brands began to sell lower-priced fashion to tween girls through its Justice stores and tween boys through its BROTHER shops.

CHANNELS Based on a target market analysis and other considerations we reviewed in Chapter 17, retailers must decide which channels to employ to reach their customers. Increasingly, the answer is multiple channels. Staples sells through its traditional retail brick-and-mortar channel, a direct-response Internet site, virtual malls, and thousands of links on affiliated sites.

As Chapter 17 also explained, channels should be designed to work together effectively. Although some experts predicted otherwise, catalogs have actually grown in an Internet world as more firms have revamped them to use them as branding devices and to complement online activity.[23] Victoria's Secret's integrated multichannel approach of retail stores, catalog, and Internet has played a key role in its brand development.[24]

VICTORIA'S SECRET Victoria's Secret, purchased by Limited Brands in 1982, has become one of the most identifiable brands in retailing through skillful marketing of women's clothing, lingerie, and beauty products. Most U.S. women a generation ago did their underwear shopping in department stores and owned few items that could be considered "lingerie." After witnessing women buying expensive lingerie as fashion items from small boutiques in Europe, Limited Brands founder Leslie Wexner felt a similar store model could work on a mass scale in the United States, though such a store format was unlike anything the average shopper would have encountered amid the bland racks at department stores. Wexner, however, had reason to believe U.S. women would relish the opportunity to have a European-style lingerie shopping experience with soft pink wallpaper, inviting fitting rooms, and attractive and attentive staff. "Women need underwear, but women want lingerie," he observed. Wexner's assumption proved correct: A little more than a decade after he bought the business, Victoria's Secret's average customer bought eight to 10 bras per year, compared with the national average of two. To enhance its upscale reputation and glamorous appeal, the brand is endorsed by high-profile supermodels in ads and televised fashion show extravaganzas. Victoria's Secret sells through its stores, Web site, and catalog, mailing 325 million U.S. catalogs a year at a cost of $200 million. Web and catalog sales account for 25 percent of the company's $5 billion in revenue. Overseas expansion is being led by "store within a store" beauty boutiques to reduce risk.

PRODUCT ASSORTMENT The retailer's product assortment must match the target market's shopping expectations in *breadth* and *depth*.[25] A restaurant can offer a narrow and shallow assortment (small lunch counters), a narrow and deep assortment (delicatessen), a broad and shallow assortment (cafeteria), or a broad and deep assortment (large restaurant).

Destination categories may play a particularly important role because they have the greatest impact on where households choose to shop and how they view a particular retailer. A supermarket could be known for the freshness of its produce or for the variety and deals its offers in soft drinks and snacks.[26]

Identifying the right product assortment can be especially challenging in fast-moving industries such as technology or fashion. At one point, Urban Outfitters ran into trouble when it strayed from its "hip but not too hip" formula, embracing new styles too quickly.[27] On the other hand, active and casual apparel retailer Aéropostale has succeeded by carefully matching its product assortment to its young teen needs.[28]

AÉROPOSTALE Fourteen- to 17-year-olds, especially those on the young end, often want to look like other teens. So while Abercrombie and American Eagle might reduce the number of cargo pants on the sales floor, Aéropostale embraces this key reality of its target market and will keep an ample supply on hand at an affordable price. Staying on top of the right trends isn't easy, but the company is among the most diligent of teen retailers when it comes to consumer research. In addition to running high-school focus groups and in-store product tests, it launched an online program that seeks the input of 10,000 of its best customers in creating new styles. An average of 3,500 participate in each of 20 tests a year. Aéropostale maintains control over its proprietary brands by designing, sourcing, marketing, and selling all its own merchandise. The company's products can be purchased only in its own stores and online. Aéropostale has gone from a lackluster performer with only 100 stores to a powerhouse with more than 1,000 outlets in the United States, Puerto Rico, and Canada. One hundred new P.S. from Aéropostale stores target 4- to 12-year-olds with a strong value emphasis. Net sales totaled more than $2.6 billion in 2012, with net sales from e-commerce contributing more than $180 billion.

Source: © Kumar Sriskandan/Alamy

Apparel retailer Aeropostale studies its young teen market carefully as it strives to stock and display the right product assortment.

The real challenge begins after defining the store's product assortment, when the retailer must develop a product-differentiation strategy. Here are some possibilities:

- ***Feature exclusive national brands not available at competing retailers.*** Saks might get exclusive rights to carry the dresses of a well-known international designer.
- ***Feature mostly private-label merchandise.*** Benetton and Gap design most of the clothes carried in their stores. Many supermarket and drug chains carry private-label merchandise.
- ***Feature blockbuster distinctive-merchandise events.*** Bloomingdale's ran a month-long celebration for the Barbie doll's 50th anniversary.
- ***Feature surprise or ever-changing merchandise.*** Off-price apparel retailer TJ Maxx offers surprise assortments of distress merchandise (goods the owner must sell immediately because it needs cash), overstocks, and closeouts sourced from more than 16,000 vendors and priced 20 percent to 60 percent below department and specialty store regular prices online and at its 1000-plus stores.
- ***Feature the latest or newest merchandise first.*** Zara excels in and profits from being first to market with appealing new looks and designs.
- ***Offer merchandise-customizing services.*** Harrods of London will make custom-tailored suits, shirts, and ties for customers in addition to ready-made menswear.
- ***Offer a highly targeted assortment.*** Lane Bryant carries goods for the larger woman. Brookstone offers unusual tools and gadgets for the person who wants to shop in a "toy store for grown-ups."

Merchandise may also vary by geographical market. Macy's and Ross Stores employ *micro-merchandising* and let managers select a significant percentage of store assortments.[29]

PROCUREMENT After deciding on the product-assortment strategy, the retailer must establish merchandise sources, policies, and practices. In the corporate headquarters of a supermarket chain, specialist buyers (sometimes called *merchandise managers*) are responsible for developing brand assortments and listening to presentations from their suppliers' salespeople.

Retailers are rapidly improving their skills in demand forecasting, merchandise selection, stock control, space allocation, and display. They use sophisticated software to track inventory, compute economic order quantities, order goods, and analyze dollars spent on vendors and products. Supermarket chains use scanner data to manage their merchandise mix on a store-by-store basis.

Some stores are using radio frequency identification (RFID) systems made up of "smart" tags—microchips attached to tiny radio antennas—and electronic readers to facilitate inventory control and product replenishment. The smart tags can be embedded on products or stuck on labels, and when the tag is near a reader, it transmits a unique identifying number to its computer database. Coca-Cola and Gillette have used them to monitor inventory and track goods in real time as they move from factories to supermarkets to shopping baskets.[30]

ALDI's unique procurement strategy emphasizes a constantly rotating group of select private label branded products.

Source: © Lisa S./Shutterstock

Stores are using **direct product profitability (DPP)** to measure a product's handling costs (receiving, moving to storage, paperwork, selecting, checking, loading, and space cost) from the time it reaches the warehouse until a customer buys it in the retail store. They learn to their surprise that the gross margin on a product often bears little relation to the direct product profit. Some high-volume products may have such high handling costs that they are less profitable and deserve less shelf space than low-volume products.

ALDI has differentiated itself on its innovative procurement strategy.[31]

ALDI The ALDI success story started in 1913 with a single small food market in Germany. Today, ALDI has two divisions, ALDI North and ALDI South, and 9,600 stores in 18 countries. While other food retailers carry thousands of products, ALDI's product range is very narrow. With about 1,000 core products, dominated by ALDI-exclusive private labels, ALDI is very focused on products with high turnover, which it can source in high quantities at low prices. Logistics, weekly promotions, and store displays of products in transport boxes are designed to keep costs as low as possible in order to provide value. Customer perception of ALDI and its products has improved significantly over the years. High quality at low prices is the brand promise, and ALDI brands have reached top ratings in many independent product tests. To its suppliers, ALDI is known as a tough but reliable partner. Price negotiations are known to be very demanding. ALDI also expects suppliers to guarantee high standards of quality, and it constantly monitors quality throughout its whole supply chain.

Source: ASSOCIATED PRESS

Target's "mass with class" assortment and pricing strategy features designers like popular entertainer Gwen Stefani.

PRICES Prices are a key positioning factor and must be set in relationship to the target market, product-and-service assortment mix, and competition.[32] All retailers would like high *turns* × *earns* (high volumes and high gross margins), but the two don't usually go together. Most retailers fall into the *high-markup, lower-volume* group (fine specialty stores) or the *low-markup, higher-volume* group (mass merchandisers and discount stores). Within each of these groups are further gradations.

At one end of the price spectrum is by-appointment-only Bijan on Rodeo Drive in Beverly Hills, known as the most expensive store in the world. The original cost of its cologne was $1,500 for six ounces, and its suits are priced at $25,000, ties at $1,200, and socks at $100.[33] At the other end of the scale, Target has skillfully combined a hip image with discount prices to offer customers a strong value proposition. It first introduced a line of products from world-renowned designers such as Michael Graves, Isaac Mizrahi, and Liz Lange and has continued to add high-profile names, such as singer Gwen Stefani to sell hip children's clothes.[34]

Most retailers will put low prices on some items to serve as traffic builders (or loss leaders) or to signal their pricing policies.[35] They will run storewide sales. They will plan markdowns on slower-moving merchandise. Shoe retailers, for example, expect to sell 50 percent of their shoes at the normal markup, 25 percent at a 40 percent markup, and the remaining 25 percent at cost. A store's average price level and discounting policies will affect its price image with consumers, but non-price-related factors such as store atmosphere and levels of service also matter.[36]

As Chapter 16 noted, some retailers such as Walmart have abandoned "sale pricing" in favor of everyday low pricing (EDLP). EDLP can lead to lower advertising costs, greater pricing stability, a stronger image of fairness and reliability, and higher retail profits. Supermarket chains practicing everyday low pricing can be more profitable than those practicing high–low sale pricing, but only in certain circumstances, such as when the market is characterized by many "large basket" shoppers who tend to buy many items on any one trip.[37]

All retailers are seeking to cut costs to improve margins. Some do so in an environmentally friendly way. Walmart has cut energy use by more than 50 percent and maintenance by more than 30 percent by painting store roofs white to reflect sunlight and reduce the use of air conditioning; capturing rain in storage tanks for flushing toilets and other uses that do not require drinking-quality water; and installing LED lights in parking lots.[38]

SERVICES Another differentiator is unerringly reliable customer service, whether face to face, across phone lines, or via online chat. Retailers must decide on the *services mix* to offer customers:

- *Prepurchase services* include accepting telephone and mail orders, advertising, window and interior display, fitting rooms, shopping hours, fashion shows, and trade-ins.
- *Postpurchase services* include shipping and delivery, gift wrapping, adjustments and returns, alterations and tailoring, installations, and engraving.
- *Ancillary services* include general information, check cashing, parking, restaurants, repairs, interior decorating, credit, rest rooms, and baby-attendant service.

Due to consumer complaints, many retailers have loosened up their returns policies in recent years. To reduce any possible impediment to sales and to improve their image with consumers, these firms are also eliminating restocking fees and extending return periods. Some policies have necessarily stayed in place, though, to combat frauds such as "wardrobing"—the practice of wearing and then returning clothing items.[39] Gift cards remain another popular service offering; consumers spend more than $100 billion on cards annually.[40]

STORE ATMOSPHERE Every store has a look and a physical layout that makes it hard or easy to move around (see "Marketing Memo: Helping Stores to Sell"). Kohl's floor plan is modeled after a racetrack loop and is designed to convey customers smoothly past all the merchandise in the store. It includes a middle aisle that hurried shoppers can use as a shortcut and yields higher spending levels than many competitors.[41]

Retailers must consider all the senses in shaping the customer's experience. Varying the tempo of music affects average time and dollars spent in the supermarket—slow music can lead to higher sales. Bloomingdale's uses different essences or scents in different departments: baby powder in the baby store; suntan lotion in the bathing suit area; lilacs in lingerie; and cinnamon and pine scent during the holiday season. Other retailers such as Victoria's Secret and Juicy Couture use their own distinctive branded perfumes, which they also sell.[42]

STORE ACTIVITIES AND EXPERIENCES The growth of e-commerce has forced traditional brick-and-mortar retailers to respond. In addition to their natural advantages, such as products that shoppers can actually see, touch, and test; real-life customer service; and no delivery lag time for most purchases, stores also provide a shopping experience as a strong differentiator.

The store atmosphere should match shoppers' basic motivations—if customers are likely to be in a task-oriented and functional mind-set, then a simpler, more restrained in-store environment may be better.[43] On the other hand, some retailers of experiential products are creating in-store entertainment to attract customers who want fun and excitement.[44] REI, seller of outdoor gear and clothing products, allows consumers to test climbing equipment on 25-foot or even 65-foot walls in the store and to try GORE-TEX raincoats under a simulated rain shower. Bass Pro Shops also offers rich customer experiences.[45]

BASS PRO SHOPS Bass Pro Shops, a retailer of outdoor sports equipment, caters to hunters, campers, fisherman, boaters, and outdoors fans of any type. Its Outdoor World superstores feature 200,000 square feet or more of giant aquariums, waterfalls, trout ponds, archery and rifle ranges, fly-tying demonstrations, indoor driving range and putting greens, and classes in everything from ice fishing to conservation—all free. Every department is set up to replicate the corresponding outdoor experience in support of product demonstrations and testing. During the summer, parents can bring their kids to the free in-store Family Summer Camp with a host of activities in all departments. Bass Pro Shops builds a strong connection to its loyal customers from the moment they enter the store—through a turnstile designed to highlight that "they are entering an attraction, not just a retail space"—and are greeted by the irreverent sign saying "Welcome Fishermen, Hunters, and Other Liars." One hundred and sixteen million people shopped at a Bass Pro Shop in 2012; the average customer drove more than 50 miles and stayed for more than two hours. The showroom in Missouri—the first and largest—is the number-one tourist destination in the state.

COMMUNICATIONS Retailers use a wide range of communication tools to generate traffic and purchases. They place ads, run special sales, issue money-saving coupons, send e-mail promotions, and run frequent-shopper-reward programs, in-store food sampling, and coupons on shelves or at check-out points. They work with manufacturers to design point-of-sale materials that reflect both their images. They time the arrival of their e-mails and design them with attention-grabbing subject lines and animation and personalized messages and advice.

Retailers are also using interactive and social media to pass on information and create communities around their brands. They study the way consumers respond to their e-mails, not only where and how messages are opened but

marketing memo

Helping Stores to Sell

In pursuit of higher sales volume, retailers are studying their store environments for ways to improve the shopper experience. Paco Underhill is a pioneer in that field and managing director of the retail consultant Envirosell, whose clients include McDonald's, Starbucks, Estée Lauder, Gap, Burger King, CVS, and Wells Fargo. Using a combination of in-store video recording and observation tracking of as many as 40 different behaviors, Underhill and his colleagues study 50,000 people each year as they shop. He offers the following advice for fine-tuning retail space:

- *Attract shoppers and keep them in the store.* The amount of time shoppers spend in a store is perhaps the single most important factor in determining how much they buy. To increase shopping time, give shoppers a sense of community; recognize them in some way; make them comfortable, such as by providing chairs in convenient locations for spouses, children, or bags; and make the environment both familiar and fresh each time they come in.
- *Honor the "transition zone."* On entering a store, people need to slow down and sort out the stimuli, which means they will likely be moving too fast to respond positively to signs, merchandise, or sales clerks in the zone they cross before making that transition. Make sure there are clear sight lines. Create a focal point for information within the store. Most right-handed people turn right upon entering a store.
- *Avoid overdesign.* Store fixtures, point-of-sales information, packaging, signage, and flat-screen televisions can combine to create a visual riot. Use crisp and clear signage—"Our Best Seller" or "Our Best Student Computer"—located where people feel comfortable stopping and facing the right way. Window signs, displays, and mannequins communicate best when angled 10 to 15 degrees to face the direction in which people are moving.
- *Don't make them hunt.* Put the most popular products up front to reward busy shoppers and encourage leisurely shoppers to look more. At Staples, ink cartridges are one of the first products shoppers encounter after entering.
- *Make merchandise available to the reach and touch.* It is hard to overemphasize the importance of customers' hands. A store can offer the finest, cheapest, sexiest goods, but if the shopper cannot reach them or pick them up, much of their appeal can be lost.
- *Make kids welcome.* If kids feel welcome, parents will follow. Take a 3-year-old's perspective and make sure there are engaging sights at eye level. A virtual hopscotch pattern or dinosaur on the floor can turn a boring shopping trip for a child into a friendly experience.
- *Note that men do not ask questions.* Men always move faster than women do through a store's aisles. In many settings, it is hard to get them to look at anything they had not intended to buy. Men also do not like asking where things are. If a man cannot find the section he is looking for, typically he will wheel about once or twice, then leave the store without ever asking for help.
- *Remember women need space.* A shopper, especially a woman, is far less likely to buy an item if her body is brushed, even lightly, by another customer when she is looking at a display. Keeping aisles wide and clear is crucial. With women playing an increasingly more significant buying role than men, designing retail experiences to satisfy them is crucial. Cleanliness, control, safety, and consideration are among the important retail decision factors for women.
- *Make check-out easy.* Be sure to have the right high-margin goods near cash registers to satisfy impulse shoppers. People love to buy candy when they check out—so satisfy their sweet tooth.

Sources: Paco Underhill, *What Women Want: The Science of Female Shopping* (New York: Simon & Schuster, 2011); Paco Underhill, *Call of the Mall: The Geography of Shopping* (New York: Simon & Schuster, 2004); Paco Underhill, *Why We Buy: The Science of Shopping* (New York: Simon & Schuster, 1999). See also Gloria Moss, "Time for Gatherers to Have More Clout in the Boardroom!," *Huffington Post*, June 3, 2012; Brian Tarren, "Watchman," *Research*, July 17, 2012; Susan Berfield, "Getting the Most Out of Every Shopper, *BusinessWeek*, February 9, 2009, pp. 45–46; Kenneth Hein, "Shopping Guru Sees Death of Detergent Aisle," *Brandweek*, March 27, 2006, p. 11.

also which words and images led to a click. Macy's segments customers into more than a dozen groups and sends different e-mails for different products.[46] Casual dining chain Houlihan's social network site, HQ, gains immediate, unfiltered feedback from 10,500 invitation-only "Houlifan" customers in return for insider information about recipes and redesigns.[47]

With 15 percent of a retailer's most loyal customers accounting for as much as half its sales, reward programs are becoming increasingly sophisticated. Consumers who choose to share personal information can receive discounts, secret or advance sales, exclusive offers, and store credits. CVS has 70 million loyalty club members who can use in-store coupon centers and receive coupons with their sales receipts.[48]

Many retailers are using Twitter to connect with customers and send ads to targeted groups.[49] Some local retailers are using digital daily-deal services from Groupon, LivingSocial, and others, although recently many have soured on the approach due to a lack of profitability.[50]

Source: Bart Ah You/ZUMApress/Newscom

Bass Pro Shops brings outdoor experiences into different departments of its stores.

LOCATION The three keys to retail success are often said to be "location, location, and location." Department store chains, oil companies, and fast-food franchisers exercise great care in selecting regions of the country in which to open outlets, then particular cities, and then particular sites. Retailers can place their stores in the following locations:

- ***Central business districts.*** The oldest and most heavily trafficked city areas, often known as "downtown"
- ***Regional shopping centers.*** Large suburban malls containing 40 to 200 stores, typically featuring one or two nationally known anchor stores, such as Macy's or Lord & Taylor or a combination of big-box stores such as PETCO, Payless Shoes, or Bed Bath & Beyond, and a great number of smaller stores, many under franchise operation.[51]
- ***Community shopping centers.*** Smaller malls with one anchor store and 20 to 40 smaller stores
- ***Shopping strips.*** A cluster of stores, usually in one long building, serving a neighborhood's needs for groceries, hardware, laundry, shoe repair, and dry cleaning
- ***A location within a larger store.*** Smaller concession spaces taken by well-known retailers like McDonald's, Starbucks, Nathan's, and Dunkin' Donuts within larger stores, airports, or schools or "store-within-a-store" specialty retailers located within a department store such as with Gucci within Neiman Marcus
- ***Stand-alone stores.*** Some retailers such as Kohl's and JCPenney are avoiding malls and shopping centers in favor of freestanding storefronts so they are not connected directly to other retail stores.

In view of the relationship between high traffic and high rents, retailers must decide on the most advantageous locations for their outlets, using traffic counts, surveys of consumer shopping habits, and analysis of competitive locations.

Private Labels

A **private-label brand** (also called a reseller, store, house, or distributor brand) is a brand that retailers and wholesalers develop. Benetton, The Body Shop, and Marks & Spencer carry mostly own-brand merchandise. In grocery stores in Europe and Canada, store brands account for as much as 40 percent of the items sold. In Britain, roughly half of what Sainsbury and Tesco, the largest food chains, sell is store-label goods. Germany and Spain are also European markets with a high percentage of private-label sales.[52]

For many manufacturers, retailers are both collaborators and competitors. According to the Private Label Manufacturers' Association, store brands now account for one of every five items sold in U.S. supermarkets, drug chains, and mass merchandisers. In one study, seven of 10 shoppers believed the private-label products they bought were as good as, if not better than, their national-brand counterparts, and virtually every household purchases private-label brands from time to time.[53] The stakes in private-label marketing are high. A one-percentage-point shift from national brands to private labels in food and beverages is estimated to add $5.5 billion in revenue for supermarket chains.[54]

Private labels are rapidly gaining ground in a way that has many manufacturers of name brands running scared. Recessions increase private-label sales, and once some consumers switch to a private label, they don't always go back.[55] But some experts believe 50 percent is the natural limit on how much private-label volume to carry because (1) consumers prefer certain national brands, and (2) many product categories are not feasible or attractive on a private-label basis. In supermarkets, private labels are big sellers in milk and cheese, bread and baked goods, medications and remedies, paper products, fresh produce, and packaged meats.[56]

ROLE OF PRIVATE LABELS

Why do intermediaries sponsor their own brands?[57] First, these brands can be more profitable. Intermediaries may be able to use manufacturers with excess capacity that will produce private-label goods at low cost. Other costs, such as research and development, advertising, sales promotion, and physical distribution, are also much lower, so private labels can generate a higher profit margin.[58] Retailers also develop exclusive store brands to differentiate themselves from competitors. Many price-sensitive consumers prefer store brands in certain categories. These preferences give retailers increased bargaining power with marketers of national brands.

We should distinguish private-label or store brands from generics. **Generics** are unbranded, plainly packaged, less expensive versions of common products such as spaghetti, paper towels, and canned peaches. They offer standard or lower quality at a price that may be as much as 20 percent to 40 percent lower than nationally advertised brands and 10 percent to 20 percent lower than the retailer's private-label brands. The lower price is made possible by lower-cost labeling and packaging and minimal advertising and sometimes lower-quality ingredients.

Generics can be found in a wide range of different products, even medicines. Pharma giant Novartis is one of the world's top five makers of branded drugs, with such successes as Diovan for high blood pressure and Gleevec for cancer, but it has also become the world's second-largest maker of generic drugs following its acquisition of Sandoz, HEXAL, Eon Labs, and others.[59]

PRIVATE-LABEL SUCCESS FACTORS

In the battle between manufacturers' and private labels, retailers have increasing market power. Because shelf space is scarce, many supermarkets charge a *slotting fee* for accepting a new brand to cover the cost of listing and stocking it. Retailers also charge for special display space and in-store advertising space. They typically give more prominent display to their own brands and make sure they are well stocked.

Retailers are building better quality into their store brands and emphasizing attractive, innovative packaging. Supermarket retailers are adding premium store-brand items. When Kroger's switched to new vendors to supply better-quality cheeses, meats, and veggies for its upscale private-label pizza, sales soared; the supermarket chain now owns 60 percent of the premium pizza market in its stores.[60] One of the most successful supermarket retailers with private labels is Canada's Loblaw.[61]

LOBLAW Since 1984, when its President's Choice line of foods made its debut, the term *private label* has brought Loblaw instantly to mind. The Toronto-based company's Decadent Chocolate Chip Cookie quickly became a Canadian leader and showed how innovative store brands could compete effectively with national brands by matching or even exceeding their quality. A finely tuned brand strategy for its premium President's Choice line and its no-frills, yellow-labeled No Name line (which the company relaunched with a vengeance during the recent recession) has helped differentiate its stores and built Loblaw into a powerhouse in Canada and the United States. The President's Choice line has become so successful that Loblaw is licensing it to noncompetitive retailers in other countries. To complete a "good, better, best" brand portfolio, Loblaw has also introduced an "affordable luxury" line of more than 200 President's Choice food products under a distinctive "Black Label" design. Each one—from eight-year-old cheddar and ginger-spiced chocolate sauce to bacon marmalade—is marketed with a story about where it's from, who produces it, and why it was chosen. To capitalize on the overall strength of its private labels, Loblaw launched a Food Network reality TV show, *Recipe to Riches*, where contestants compete to have their homemade recipes developed into an actual President's Choice product available to purchase the very next day at Loblaw's stores.

Although retailers get credit for the success of private labels, the growing power of store brands has also benefited from the weakening of national brands. Many consumers have become more price sensitive, a trend reinforced by the continuous barrage of coupons and price specials that has trained a generation to buy on price. Competing manufacturers and national retailers copy and duplicate the quality and features of the best brands in marketing insight

Manufacturer's Response to the Private-Label Threat

To stay a step ahead of store brands, leading brand marketers are investing significantly in R&D to bring out new brands, line extensions, features, and quality improvements. They are also investing in strong "pull" advertising programs to maintain high brand recognition and consumer preference and to overcome the in-store marketing advantage private labels can enjoy.

Top-brand marketers also are seeking to partner with major mass distributors in a joint search for logistical economies and competitive strategies that produce savings for both sides. Cutting all unnecessary costs allows national brands to command a price premium, though price can't exceed consumers' perception of value.

Creating strong consumer demand is crucial. When Walmart decided to pull Hefty and Glad food bags from its shelves, selling just Ziploc and its own Great Value brand, Hefty and Glad stood to lose because the retail giant accounted for a third of their sales. When consumers complained about the loss of these and other brands and switched some of their shopping to other stores, Walmart relented and put them back on the shelves.

Effective positioning is crucial. Despite holding a hefty 60 percent price premium over its private-label competitors, Pepto-Bismol gained market share during the recession. A clever advertising campaign portraying the product as an effective multipurpose "insurance policy" for gastrointestinal maladies struck a chord with value-minded consumers.

University of North Carolina's Jan-Benedict E. M. Steenkamp and London Business School's Nirmalya Kumar offer four strategic recommendations for manufacturers to compete against or collaborate with private labels.

- *Fight selectively* when manufacturers can win against private labels and add value for consumers, retailers, and shareholders. This typically occurs when the brand is number one or two in the category or occupying a premium niche position. Procter & Gamble rationalized its portfolio, selling off various brands such as Sunny Delight juice drink, Jif peanut butter, and Crisco shortening, in part so it could concentrate on strengthening its 20-plus brands with more than $1 billion in sales.
- *Partner effectively* by seeking win-win relationships with retailers through strategies that complement the retailer's private labels. Estée Lauder created four brands (American Beauty, Flirt, Good Skin, and Grassroots) exclusively for Kohl's to help the retailer generate volume and protect its more prestigious brands in the process. Manufacturers selling through hard discounters such as Lidl and Aldi have increased sales by finding new customers who have not previously bought the brand.
- *Innovate brilliantly* with new products to help beat private labels. Continuously launching incrementally new products keeps the manufacturer brands looking fresh, but the firm must also periodically launch radically new products and protect the intellectual property of all brands. Kraft doubled its number of patent lawyers to make sure its innovations were legally protected as much as possible.
- *Create winning value propositions* by imbuing brands with symbolic imagery as well as functional quality that beats private labels. Too many manufacturer brands have let private labels equal and sometimes better them on functional quality. In addition, to have a winning value proposition, marketers need to monitor pricing and ensure that perceived benefits equal the price premium.

Sources: Tony Fanin, "Brands Still Mean Something at Walmart," www.bebranded.wordpress.com, March 22, 2010; Parija Kavilanz, "Dumped! Brand Names Fight to Stay in Stores," *USA Today,* February 16, 2010; Jan-Benedict E. M. Steenkamp and Nirmalya Kumar, "Don't Be Undersold," *Harvard Business Review*, December 2009, p. 91; Jack Neff, "Pepto Beats Private Label despite 60% Price Premium," *Wall Street Journal*, September 21, 2009; Nirmalya Kumar and Jan-Benedict E. M. Steenkamp, *Private Label Strategy: How to Meet the Store-Brand Challenge* (Boston: Harvard Business School Press, 2007); Nirmalya Kumar, "The Right Way to Fight for Shelf Domination," *Advertising Age*, January 22, 2007; James A. Narus and James C. Anderson, "Contributing as a Distributor to Partnerships with Manufacturers," *Business Horizons* (September–October 1987).

a category, reducing physical product differentiation. Moreover, by cutting marketing communication budgets, some firms have made it harder to create any intangible differences in brand image. A steady stream of brand extensions and line extensions has blurred brand identity at times and led to a confusing amount of product proliferation.

Bucking these trends, many manufacturers or national brands are fighting back. "Marketing Insight: Manufacturer's Respond to the Private-Label Threat," describes the strategies and tactics being taken to compete more effectively with private labels.[62]

Wholesaling

Wholesaling includes all the activities in selling goods or services to those who buy for resale or business use. It excludes manufacturers and farmers because they are engaged primarily in production, and it excludes retailers. The major types of wholesalers are described in Table 18.4.

TABLE 18.4	Major Wholesaler Types
	Merchant wholesalers: Independently owned businesses that take title to the merchandise they handle. They are full-service and limited-service jobbers, distributors, and mill supply houses.
	Full-service wholesalers: Carry stock, maintain a sales force, offer credit, make deliveries, provide management assistance. Wholesale merchants sell primarily to retailers: Some carry several merchandise lines, some carry one or two lines, others carry only part of a line. Industrial distributors sell to manufacturers and also provide services such as credit and delivery.
	Limited-service wholesalers: *Cash and carry wholesalers* sell a limited line of fast-moving goods to small retailers for cash. *Truck wholesalers* sell and deliver a limited line of semiperishable goods to supermarkets, grocery stores, hospitals, restaurants, and hotels. *Drop shippers* serve bulk industries such as coal, lumber, and heavy equipment. They assume title and risk from the time an order is accepted to its delivery. *Rack jobbers* serve grocery retailers in nonfood items. Delivery people set up displays, price goods, and keep inventory records; they retain title to goods and bill retailers only for goods sold to the end of the year. *Producers' cooperatives* assemble farm produce to sell in local markets. *Mail-order wholesalers* send catalogs to retail, industrial, and institutional customers; orders are filled and sent by mail, rail, plane, or truck.
	Brokers and agents: Facilitate buying and selling, on commission of 2 percent to 6 percent of the selling price; limited functions; generally specialize by product line or customer type. *Brokers* bring buyers and sellers together and assist in negotiation; they are paid by the party hiring them—food brokers, real estate brokers, insurance brokers. *Agents* represent buyers or sellers on a more permanent basis. Most manufacturers' agents are small businesses with a few skilled salespeople: Selling agents have contractual authority to sell a manufacturer's entire output; purchasing agents make purchases for buyers and often receive, inspect, warehouse, and ship merchandise; commission merchants take physical possession of products and negotiate sales.
	Manufacturers' and retailers' branches and offices: Wholesaling operations conducted by sellers or buyers themselves rather than through independent wholesalers. Separate branches and offices are dedicated to sales or purchasing. Many retailers set up purchasing offices in major market centers.
	Specialized wholesalers: Agricultural assemblers (buy the agricultural output of many farms), petroleum bulk plants and terminals (consolidate the output of many wells), and auction companies (auction cars, equipment, etc., to dealers and other businesses).

Wholesalers (also called *distributors*) differ from retailers in a number of ways. First, wholesalers pay less attention to promotion, atmosphere, and location because they are dealing with business customers rather than final consumers. Second, wholesale transactions are usually larger than retail transactions, and wholesalers usually cover a larger trade area than retailers. Third, wholesalers and retailers are subject to different legal regulations and taxes.

Why do manufacturers not sell directly to retailers or final consumers? Why use wholesalers at all? In general, wholesalers can more efficiently perform one or more of the following functions:

- ***Selling and promoting.*** Wholesalers' sales forces help manufacturers reach many small business customers at a relatively low cost. They have more contacts, and buyers often trust them more than they trust a distant manufacturer.
- ***Buying and assortment building.*** Wholesalers are able to select items and build the assortments their customers need, saving them considerable work.
- ***Bulk breaking.*** Wholesalers achieve savings for their customers by buying large carload lots and breaking the bulk into smaller units.
- ***Warehousing.*** Wholesalers hold inventories, thereby reducing inventory costs and risks to suppliers and customers.
- ***Transportation.*** Wholesalers can often provide quicker delivery to buyers because they are closer to the buyers.
- ***Financing.*** Wholesalers finance customers by granting credit and finance suppliers by ordering early and paying bills on time.

- ***Risk bearing.*** Wholesalers absorb some risk by taking title and bearing the cost of theft, damage, spoilage, and obsolescence.
- ***Market information.*** Wholesalers supply information to suppliers and customers regarding competitors' activities, new products, price developments, and so on.
- ***Management services and counseling.*** Wholesalers often help retailers improve their operations by training sales clerks, helping with store layouts and displays, and setting up accounting and inventory-control systems. They may help industrial customers by offering training and technical services.

TRENDS IN WHOLESALING

Wholesaler-distributors have faced mounting pressures in recent years from new sources of competition, demanding customers, new technologies, and more direct-buying programs by large industrial, institutional, and retail buyers. Manufacturers' major complaints against wholesalers are: They don't aggressively promote the manufacturer's product line and they act more like order takers; they don't carry enough inventory and therefore don't fill customers' orders fast enough; they don't supply the manufacturer with up-to-date market, customer, and competitive information; they don't attract high-caliber managers to bring down their own costs; and they charge too much for their services.

Savvy wholesalers have rallied to the challenge and adapted their services to meet their suppliers' and target customers' changing needs. They recognize that they must add value to the channel. Arrow Electronics has done just that.[63]

ARROW ELECTRONICS Arrow Electronics is a global provider of products, services, and solutions to the electronic component and computer product industries. It serves as a supply-channel partner for more than 100,000 original-equipment manufacturers, contract manufacturers, and commercial customers through a global network of 470 locations in 55 countries and territories. With huge contract manufacturers buying more parts directly from suppliers, however, distributors like Arrow are being squeezed out. To better compete, the company has embraced services, providing financing, on-site inventory management, parts-tracking software, and chip programming. Services helped quadruple its share price over a five-year stretch, and the company topped $21.4 billion in sales in 2013.

Wholesalers have worked to increase asset productivity by better managing inventories and receivables. They're also reducing operating costs by investing in more advanced materials-handling technology, information systems, and the Internet. Finally, they're improving their strategic decisions about target markets, product assortment and services, price, communications, and distribution.

Academic experts Jim Narus and Jim Anderson interviewed leading industrial distributors and identified four ways they strengthened their relationships with manufacturers:[64]

1. They sought a clear agreement with their manufacturers about their expected functions in the marketing channel.
2. They gained insight into the manufacturers' requirements by visiting their plants and attending manufacturer association conventions and trade shows.
3. They fulfilled their commitments to the manufacturer by meeting the volume targets, paying bills promptly, and feeding back customer information to their manufacturers.
4. They identified and offered value-added services to help their suppliers.

The wholesaling industry remains vulnerable to one of the most enduring trends—fierce resistance to price increases and the winnowing out of suppliers based on cost and quality. The trend toward vertical integration, in which manufacturers try to control or own their intermediaries, is still strong.

Market Logistics

Physical distribution starts at the factory. Managers choose a set of warehouses (stocking points) and transportation carriers that will deliver the goods to final destinations in the desired time or at the lowest total cost. Physical distribution has now been expanded into the broader concept of **supply chain management (SCM)**. Supply chain management starts before physical distribution and includes strategically procuring the right inputs (raw materials, components, and capital equipment), converting them efficiently into finished products, and dispatching them to the final destinations. An even broader perspective looks at how the company's suppliers themselves obtain their inputs.

The supply chain perspective can help a company identify superior suppliers and distributors and then help it improve productivity and reduce costs. Firms with top supply chains include Apple, McDonald's, Amazon.com, Unilever, Intel, Procter & Gamble, Cisco Systems, and Samsung Electronics.[65] Some companies choose to partner with and outsource to third-party logistics specialists for help with transportation planning, distribution center management, and other valued-added services that go beyond shipping and storing.[66]

Getting the supply chain right can have huge payoffs. In 2005, Whirlpool found itself with a hodgepodge of warehouses, transport depots, and factory-distribution centers. After a four-year, $600 million investment in a new state-of-the-art distribution system built from scratch, the company reduced its annual inventory by about $250 million a year and now realizes a savings of $100 million a year in increased efficiency while being able to deliver products in 48 to 72 hours.[67]

Market logistics includes planning the infrastructure to meet demand, then implementing and controlling the physical flows of materials and final goods from points of origin to points of use to meet customer requirements at a profit. Market logistics planning has four steps:[68]

1. Deciding on the company's value proposition to its customers. (What on-time delivery standard should we offer? What levels should we attain in ordering and billing accuracy?)
2. Selecting the best channel design and network strategy for reaching the customers. (Should the company serve customers directly or through intermediaries? What products should we source from which manufacturing facilities? How many warehouses should we maintain, and where should we locate them?)
3. Developing operational excellence in sales forecasting, warehouse management, transportation management, and materials management
4. Implementing the solution with the best information systems, equipment, policies, and procedures

Studying market logistics leads managers to find the most efficient way to deliver value. For example, a software company traditionally produced and packaged software disks and manuals, shipped them to wholesalers, which shipped them to retailers, which sold them to customers, who brought them home to download onto their PCs. Market logistics offered two superior delivery systems. The first let the customer download the software directly onto his or her computer. The second allowed the computer manufacturer to download the software onto its products. Both solutions eliminated the need for printing, packaging, shipping, and stocking millions of disks and manuals and have quickly become the norm of the industries.

INTEGRATED LOGISTICS SYSTEMS

The market logistics task calls for **integrated logistics systems (ILS)**, which include materials management, material flow systems, and physical distribution, aided by information technology (IT). Information systems play a critical role in managing market logistics, especially via computers, point-of-sale terminals, uniform product bar codes, satellite tracking, electronic data interchange (EDI), and electronic funds transfer (EFT). These developments have shortened the order-cycle time, reduced clerical labor, reduced errors, and provided improved control of operations. They have enabled companies to promise "the product will be at dock 25 at 10:00 AM tomorrow" and to deliver on that promise.

Market logistics encompass several activities. The first is sales forecasting, on the basis of which the company schedules distribution, production, and inventory levels. Production plans indicate the materials the purchasing department must order. These materials arrive through inbound transportation, enter the receiving area, and are stored in raw-material inventory. Raw materials are converted into finished goods. Finished-goods inventory is the link between customer orders and manufacturing activity. Customers' orders draw down the finished-goods inventory level, and manufacturing activity builds it up. Finished goods flow off the assembly line and pass through packaging, in-plant warehousing, shipping-room processing, outbound transportation, field warehousing, and delivery and service.

Management has become concerned about the total cost of market logistics, which can amount to as much as 30 to 40 percent of the product's cost. In the U.S. grocery business, waste or "shrink" affects 8 to 10 percent of perishable goods, costing $20 billion annually. Stop & Shop, a $16 billion grocery chain, discovered that large, mountainous displays of fruits and veggies and other perishables don't necessarily equal more sales. Instead it often led to spoilage on the shelf, displeasing customers and requiring more staff to sort out the perished items. After an analysis of the perishable departments, Stop & Shop cut the number of foods on display—8 avocados instead of 24, 4 salmon filets instead of 12, for example—and saved an estimated annual $100 million by reducing shrink and improving customer satisfaction.[69]

Source: Stop & Shop

By cutting the number of perishable fruits and vegetables on display, Stop & Shop saves an estimated $100 million annually.

Many experts call market logistics "the last frontier for cost economies," and firms are determined to wring every unnecessary cost out of the system: In 1982, logistics represented 14.5 percent of U.S. GDP; by 2012, the share had dropped to about 8.5 percent.[70] Lowering these costs yields lower prices, higher profit margins, or both. Even though the cost of market logistics can be high, a well-planned program can be a potent tool in competitive marketing.

Many firms are embracing **lean manufacturing**, originally pioneered by Japanese firms such as Toyota, to produce goods with minimal waste of time, materials, and money. CONMED's disposable devices are used by a hospital somewhere in the world every 90 seconds to insert and remove fluid around joints during orthoscopic surgery.[71]

CONMED To streamline production, medical manufacturer CONMED set out to link its operations as closely as possible to the ultimate buyer of its products, applying lean manufacturing and Six Sigma philosophies to boost productivity, improve its use of floor space, and cut inventory. Rather than moving manufacturing to China, which might have lowered labor costs but could have also risked long lead times, inventory buildup, and unanticipated delays, the firm put new production processes into place to assemble its disposable products only after hospitals placed orders. Some 80 percent of orders were predictable enough that demand forecasts updated every few months could set hourly production targets. As proof of CONMED's new efficiency, the assembly area for fluid-injection devices went from covering 3,300 square feet and stocking $93,000 worth of parts to 650 square feet and $6,000 worth of parts. Output per worker increased 21 percent. Similarly, its shaver blade factory increased production while decreasing costs by as much as 30 percent in some cases.

Lean manufacturing must be implemented thoughtfully and monitored closely. Toyota's crisis in product safety, which resulted in extensive product recalls, has been attributed in part to the fact that some aspects of lean manufacturing—eliminating overlap by using common parts and designs across multiple product lines and reducing the number of suppliers to procure parts with greater economies of scale—can backfire when quality-control issues arise.[72]

MARKET-LOGISTICS OBJECTIVES

Many companies state their market-logistics objective as "getting the right goods to the right places at the right time for the least cost." Unfortunately, this objective provides little practical guidance. No system can simultaneously maximize customer service and minimize distribution cost. Maximum customer service implies large inventories, premium transportation, and multiple warehouses, all of which raise market-logistics costs.

Nor can a company achieve market-logistics efficiency by asking each market-logistics manager to minimize his or her own logistics costs. Market-logistics costs interact and are often negatively related. For example:

- The traffic manager favors rail shipment over air shipment because rail costs less. However, because the railroads are slower, rail shipment ties up working capital longer, delays customer payment, and might send customers to competitors who offer faster service.
- The shipping department uses cheap containers to minimize shipping costs. Cheaper containers lead to a higher rate of damaged goods and customer ill will.
- The inventory manager favors low inventories. This increases stock-outs, back orders, paperwork, special production runs, and high-cost, fast-freight shipments.

Given these trade-offs, managers must make decisions on a total-system basis. The starting point is to study what customers require and what competitors are offering. Customers are interested in on-time delivery, help meeting emergency needs, careful handling of merchandise, and quick return and replacement of defective goods.

The wholesaler must then research the relative importance of these service outputs. For example, service-repair time is very important to buyers of copying equipment. Xerox developed a service delivery standard that "can put a disabled machine anywhere in the continental United States back into operation within three hours after receiving the service request." It then designed a service division of technicians, parts, and locations to deliver on this promise.

The company must also consider competitors' service standards. It will normally want to match or exceed these, but the objective is to maximize profits, not sales. Some companies offer less service and charge a lower price; other companies offer more service and charge a premium price.

The company ultimately must establish some promise it makes to the market. Some companies define standards for each service factor. One appliance manufacturer promises to deliver at least 95 percent of the dealer's orders within seven days of order receipt, to fill them with 99 percent accuracy, to deal with inquiries about order status within three hours, and to ensure that merchandise damaged in transit does not exceed 1 percent.

MARKET-LOGISTICS DECISIONS

The firm must make four major decisions about its market logistics: (1) How should we handle orders (order processing)? (2) Where should we locate our stock (warehousing)? (3) How much stock should we hold (inventory)? and (4) How should we ship goods (transportation)?

ORDER PROCESSING Most companies today are trying to shorten the *order-to-payment cycle*—that is, the time between an order's receipt, delivery, and payment. This cycle has many steps, including order transmission by the salesperson, order entry and customer credit check, inventory and production scheduling, order and invoice shipment, and receipt of payment. The longer this cycle takes, the lower the customer's satisfaction and the lower the company's profits.

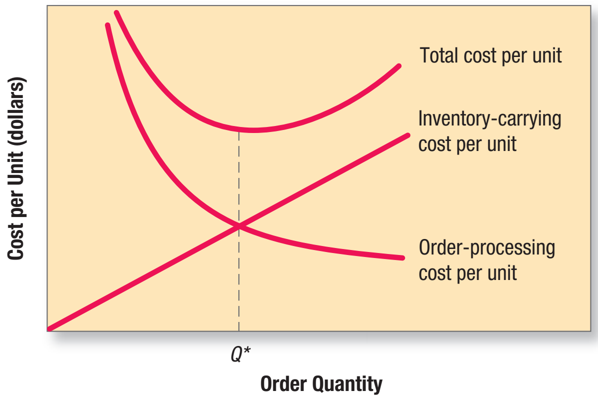
WAREHOUSING Every company must store finished goods until they are sold because production and consumption cycles rarely match. More stocking locations mean goods can be delivered to customers more quickly, but warehousing and inventory costs are higher. To reduce these costs, the company might centralize its inventory in one place and use fast transportation to fill orders. To better manage inventory, many department stores such as Nordstrom and Macy's now ship online orders from individual stores.[73]

Some warehouses are now taking on activities formerly done in the plant, including product assembly, packaging, and construction of promotional displays. Moving these activities to the warehouse can save costs and match the offerings more closely to demand.

INVENTORY Salespeople would like their companies to carry enough stock to fill all customer orders immediately. However, this is not cost effective. Inventory cost increases at an accelerating rate as the customer-service level approaches 100 percent. Management needs to know how much sales and profits would increase as a result of carrying larger inventories and promising faster order fulfillment times and then make a decision.

As inventory draws down, management must know at what stock level to place a new order. This stock level is called the *order* (or *reorder*) *point*. An order point of 20 means reordering when the stock falls to 20 units. The order point should balance the risks of stock-out against the costs of overstock. The other decision is how much to order. The larger the quantity ordered, the less frequently an order needs to be placed.

The company needs to balance order-processing costs and inventory-carrying costs. *Order-processing costs* for a manufacturer consist of *setup costs* and *running costs* (operating costs when production is running) for the item. If setup costs are low, the manufacturer can produce the item often, and the average cost per item is stable and



| Fig. 18.1 |

Determining Optimal Order Quantity

equal to the running costs. If setup costs are high, however, the manufacturer can reduce the average cost per unit by producing a long run and carrying more inventory.

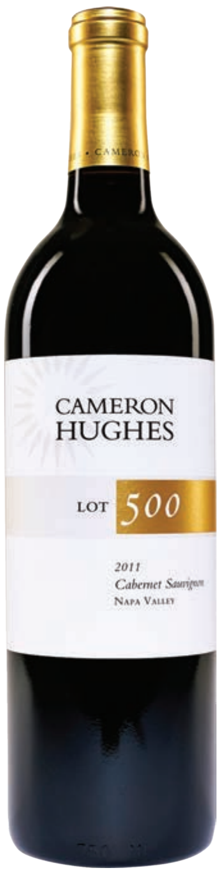
Order-processing costs must be compared with *inventory-carrying costs,* which include storage charges, cost of capital, taxes and insurance, and depreciation and obsolescence. Carrying costs might run as high as 30 percent of inventory value and are higher the larger the average stock carried. This means marketing managers who want to carry larger inventories need to show that incremental gross profits will exceed incremental carrying costs.

We can determine the optimal order quantity by observing how order-processing costs and inventory-carrying costs add up at different order levels. Figure 18.1 shows that the order-processing cost per unit decreases as the number of units ordered increases because the order costs are spread over more units. Inventory-carrying charges per unit increase with the number of units ordered because each unit remains longer in inventory. We sum the two cost curves vertically into a total-cost curve and project the lowest point of the total-cost curve on the horizontal axis to find the optimal order quantity Q^*.[74]

Companies are reducing their inventory costs by treating inventory items differently, keeping slow-moving items in a central location and carrying fast-moving items in warehouses closer to customers. Managers are also considering inventory strategies that give them flexibility should anything go wrong, as it often does, whether a dock strike in California, an earthquake in Japan, or political turmoil in North Africa and the Middle East. In an interconnected world, one weak link, if not properly managed, can bring down the entire supply chain.[75]

The ultimate answer to carrying *near-zero inventory* is to build for order, not for stock. Sony calls it SOMO, "Sell one, make one." Dell's inventory strategy for years has been to get the customer to order a computer and pay for it in advance. Then Dell uses the customer's money to pay suppliers to ship the necessary components. As long as customers do not need the item immediately, everyone can save money. Some retailers are unloading excess inventory on eBay where, by cutting out the liquidator middleman, they can make 60 to 80 cents on the dollar as opposed to 10 cents.[76] And some suppliers are snapping up excess inventory to create opportunity.[77]

CAMERON HUGHES "If a winery has an eight-barrel lot, it may only use five barrels for its customers," says Cameron Hughes, a wine *négociant* who buys excess juice from high-end wineries and wine brokers in France, Italy, Spain, Argentina, South Africa, and California and combines it to make limited-edition, premium blends that taste much more expensive than their price tags. A $100 California Cabernet may sell for $25 a bottle or less under his Lot 500 Napa Valley Cabernet Savignon label. *Négociants* have been around a long time, first as intermediaries who sold or shipped wine as wholesalers, but the profession has expanded as opportunists such as Hughes began making their own wines. Hughes doesn't own any grapes, bottling machines, or trucks. He outsources the bottling, and he sells directly to retailers such as Costco, Sam's Club, and Safeway, eliminating intermediaries and multiple markups. Hughes never knows which lots of wine he will have or how many, but he's turned uncertainty to his advantage—he creates a new product with every batch. Rapid turnover is part of Costco's appeal for him. The discount store's customers love the idea of finding a rare bargain, and Hughes promotes his wines through in-store wine tastings and insider e-mails about his upcoming numbered lots, which sell out quickly. One thing customers won't find out is exactly where the wine comes from. In signing deals Hughes typically has to accept non-disclosure agreements prohibiting him from naming his sources, though the Cameron Confidential flyer that accompanies each wine may hint at it.



Source: Cameron Hughes Wine

Cameron Hughes buys excess juice to make and sell affordable, high quality wines to select merchants.

TRANSPORTATION Transportation choices affect product pricing, on-time delivery performance, and the condition of the goods when they arrive, all of which affect customer satisfaction.

In shipping goods to its warehouses, dealers, and customers, a company can choose rail, air, truck, waterway, or pipeline. Shippers consider such criteria as speed, frequency, dependability, capability, availability, traceability, and cost. For speed, the prime contenders are air, rail, and truck. If the goal is low cost, then the choice is water or pipeline.

Shippers are increasingly combining two or more transportation modes, thanks to containerization. **Containerization** consists of putting the goods in boxes or trailers that are easy to transfer between two transportation modes. *Piggyback* describes the use of rail and trucks; *fishyback,* water and trucks; *trainship,* water and rail; and *airtruck,* air and trucks. Each coordinated mode offers specific advantages. For example, piggyback is cheaper than trucking alone yet provides flexibility and convenience.

Shippers can choose private, contract, or common carriers. If the shipper owns its own truck or air fleet, it becomes a *private carrier.* A *contract carrier* is an independent organization selling transportation services to others on a contract basis. A *common carrier* provides services between predetermined points on a scheduled basis and is available to all shippers at standard rates. Some contract carriers are investing and innovating to create strong value propositions.[78]

CONTRACT CARRIERS With so many transportation options available, firms in those industries are constantly competing to cut costs, improve services, and offer even more value to their shipping customers. After 10 years and billions of dollars in investment, including $2.5 billion in 2010 alone, Union Pacific saw on-time delivery on its railroads increase from 30 percent to roughly 90 percent. Improving reliability is also important in ocean shipping. Copenhagen-based Maersk Group is the world's largest global shipper, with around 550 container ships and 225 tankers. To improve efficiency, the firm in 2014 commissioned 20 of the largest ships ever built. Costing $185 million each, these giant ships can cost-effectively carry 18,000 containers, also emitting 50 percent less CO_2 in the process. Schneider, one of the country's largest full-truckload freight haulers with more than $3 billion in revenue, developed a fleet-wide "tactical simulator" that has saved the company tens of millions of dollars. Besides helping in the crucial day-to-day route scheduling for drivers, the simulator has also helped with specific decisions ranging from when to raise prices for certain customers to how many drivers to hire (and where). Little changes can make big differences for shippers. Global logistics leader UPS calculated that by having its drivers use a fob instead of a key to operate its trucks, it is cutting out on average 1.7 seconds per stop, or 6.5 minutes per day, saving an estimated $70 million a year in the process.

Union Pacific has invested billions to improve its on-time delivery.

Source: © Stephen Jonas/Alamy

Source: A.P. Møller-Mærsk A/S

Global shipping leader Maersk commissioned 20 of the largest, efficient ships ever built.

To reduce costly handing at arrival, some firms are putting items into shelf-ready packaging so they don't have to unpack them from a box and place them individually on a shelf. In Europe, P&G has used a three-tier logistic system to schedule deliveries of fast- and slow-moving goods, bulky items, and small items in the most efficient way.[79] To reduce damage in shipping, the size, weight, and fragility of the item must be reflected in the crating technique used and the density of foam cushioning.[80] With logistics, every little detail must be reviewed to see how it might be changed to improve productivity and profitability.

Summary

1. Retailing includes all the activities in selling goods or services directly to final consumers for personal, non-business use. Retailers can be store retailers, nonstore retailers, and retail organizations.
2. Retailers pass through stages of growth and decline. As existing stores offer more services to remain competitive, costs and prices go up, which opens the door to new retail forms that offer merchandise and services at lower prices. The major types of retail stores are specialty stores, department stores, supermarkets, convenience stores, discount stores, extreme value or hard-discount store, off-price retailers, superstores, and catalog showrooms.
3. Nonstore retailing is growing and includes direct selling (one-to-one selling, one-to-many party selling, and multilevel network marketing), direct marketing (which includes e-commerce and Internet retailing), automatic vending, and buying services.
4. Retail organizations achieve many economies of scale, greater purchasing power, wider brand recognition, and better-trained employees. The major types of corporate retailing are corporate chain stores, voluntary chains, retailer cooperatives, consumer cooperatives, franchise organizations, and merchandising conglomerates.
5. As new retail forms have emerged, competition between them has increased, the rise of giant retailers has been matched by the decline of middle-market retailers, investment in technology has grown, and shopper marketing inside stores has become a priority.
6. Like all marketers, retailers must prepare marketing plans that include decisions about target markets, channels, product assortment and procurement, prices, services, store atmosphere, store activities and experiences, communications, and location.
7. Wholesaling includes all the activities in selling goods or services to those who buy for resale or business use. Wholesalers can perform functions better and more cost-effectively than the manufacturer can. These functions include selling and promoting, buying and assortment building, bulk breaking, warehousing, transportation, financing, risk bearing, dissemination of market information, and provision of management services and consulting.
8. There are four types of wholesalers: merchant wholesalers; brokers and agents; manufacturers' and retailers' sales branches, sales offices, and purchasing offices; and miscellaneous wholesalers such as agricultural assemblers and auction companies.

9. Like retailers, wholesalers must decide on target markets, product assortment and services, price, promotion, and place. The most successful are those that adapt their services to meet suppliers' and target customers' needs.
10. Producers of physical products and services must decide on market logistics—the best way to store and move goods and services to market destinations and to coordinate the activities of suppliers, purchasing agents, manufacturers, marketers, channel members, and customers. Major gains in logistical efficiency have come from advances in information technology.

MyMarketingLab

Go to **mymktlab.com** to complete the problems marked with this icon ✪ as well as for additional Assisted-graded writing questions.

Applications

Marketing Debate

Should National-Brand Manufacturers Also Supply Private-Label Brands?

Ralston-Purina, Borden, ConAgra, and Heinz have all admitted at some point to supplying products—sometimes lower in quality—to be used for private labels. Other marketers, however, criticize this "if you can't beat them, join them" strategy, maintaining that these actions, if revealed, may create confusion or even reinforce a perception by consumers that all brands in a category are essentially the same.

Take a position: **Manufacturers should feel free to sell private labels as a source of revenue *versus* National manufacturers should never supply private labels.**

Marketing Discussion

Retail Customer Loyalty

✪ Think of your favorite stores. What do they do that encourages your loyalty? What do you like about the in-store experience? What further improvements could these stores make?

Marketing Excellence

>> Zara

Zara, the Spanish-based company, is Europe's leading apparel retailer, providing consumers with current, high-fashion styles at reasonable prices. With more than $14.5 billion in sales and more than 2,000 stores, the company has succeeded by breaking virtually every traditional rule in the retailing industry.

The first Zara store opened in 1975. By the 1980s, founder Amancio Ortega was working with computer programmers on a new distribution model to reduce the time from design to distribution to just two weeks—a groundbreaking difference from the industry average of six to nine months. As a result, the company now makes between 10,000 and 20,000 different items a year, approximately triple the number made by Gap or H&M. With this revolutionary step, Zara was able to introduce "fast fashion" at affordable prices.

Zara's business model is keenly focused on four strategic elements:

Design and Production. Zara employs hundreds of designers at its headquarters in Spain. Thus, new styles are constantly being created and put into production while others are tweaked with various colors or patterns. The firm enforces the speed at which it puts these designs into production by locating half its production facilities nearby in Spain, Portugal, and Morocco. It produces only a small quantity of each collection and is willing to experience occasional shortages to preserve an image of exclusivity. Clothes with a longer shelf life, like T-shirts, are outsourced to lower-cost suppliers in Asia and Turkey. With tight control on its manufacturing process, Zara can move more rapidly than any of its competitors and continues to deliver fresh styles to its stores every week.

Logistics. Zara distributes all its merchandise, regardless of origin, from Spain. Its distribution process is designed so that the time from receipt of an order to delivery in the store averages 24 hours in Europe and 48 hours in the United States and Asia. Having 50 percent of its production facilities nearby is key to the success of this model. All Zara stores receive new shipments twice a week, and the small quantities of each collection entice consumers not only to return frequently but also to make purchase decisions more quickly. Because of its logistics and inventory policy, while an average shopper in Spain visits a main street store three times a year, shoppers to a Zara store average 17 trips. Some fans know exactly what day new shipments arrive and show up early to be the first in line, keeping the company's sales strong throughout the year and even during slow economic times. The company also sells more products at full price—85 percent of its merchandise versus the industry average of 60 percent.

Customers. Everything revolves around Zara's customers. The retailer monitors customers' changing needs, trends, and tastes through daily reports from shop managers about which products and styles have sold and which haven't. Managers earn as much as 70 percent of their salaries from commission, so they have a strong incentive to stay on top of things. Zara's designers don't have to predict what fashion trends will be in the future. They react to customer feedback—good and bad—and if an idea fails, the line is withdrawn immediately. Zara cuts its losses and the impact is minimal due to the small quantities of each style produced.

Stores. Zara does not run advertising campaigns. The retailer's stores, in prestigious high-traffic locations around the world, are its key advertising element, featuring stylish and constantly changing window displays. Other retailers spend 3 percent to 4 percent of revenues on big brand-building campaigns, while Zara spends just 0.3 percent. The company has said it would rather use a percentage of revenue to open new stores than to advertise.

Zara's success comes from having complete control over all the parts of its business—design, production, and distribution. Louis Vuitton's fashion director, Daniel Piette, described the company as "possibly the most innovative and devastating retailer in the world." It has expanded aggressively throughout Europe as well as into emerging markets such as Asia, the Americas, and the Middle East, making sure it honors local tastes in each region. Zara was a latecomer to the Internet and launched its first online store only in 2011. However, the company now uses its Web site to test the waters before entering potential markets like China, Russia, and Canada with retail storefronts.

While Zara has experience record sales as of late, it faces unique challenges ahead, including what to do in the United States, where obesity rates are much higher than in the rest of the world and roomy clothes are preferred to the slim fits and high fashion the company offers. It also needs to decide how to maintain its tight control on manufacturing as it expands throughout the world.

Questions

1. Would Zara's model work for other retailers? Why or why not?
2. What can Zara do to ensure successful growth around the world while maintaining the same level of speed and instant fashion?

Sources: Rachel Tiplady, "Zara: Taking the Lead in Fast-Fashion," *BusinessWeek*, April 4, 2006; enotes.com, Inditex overview; "Zara: A Spanish Success Story," *CNN*, June 15, 2001; "Fashion Conquistador," *BusinessWeek*, September 4, 2006; Caroline Raux, "The Reign of Spain," *The Guardian*, October 28, 2002; Kerry Capell, "Zara Thrives by Breaking All the Rules," *BusinessWeek*, October 20, 2008, p. 66; Christopher Bjork, "Zara Is to Get Big Online Push," *Wall Street Journal*, September 17, 2009, p. B8; "Best Global Brands 2013," *Interbrand;* Walter Loeb, "Zara's Secret to Success: The New Science of Retailing," *Forbes*, October 14, 2013; Jessica Sheft-Ason, "Zara to Launch Online Shopping in September," *Forbes*, August 3, 2011; Zara.com; Inditex 2012 Annual Report.

Marketing Excellence

>> Best Buy

Best Buy is the world's largest multichannel consumer electronics retailer, with $45 billion in sales in fiscal 2013. Sales boomed in the 1980s as the company expanded nationally and made some risky business decisions, like putting its sales staff on salary instead of commission. This decision created a more consumer-friendly, low-pressure shopping atmosphere and resulted in an instant spike in overall revenues. In the 1990s, Best Buy ramped up its computer product offerings, and by 1995 it was the biggest seller of home PCs, a powerful market position during the Internet boom.

At the turn of the 21st century, Best Buy faced new retail competitors, including Costco, Walmart, and Target, which boosted their electronics divisions and product offerings and often priced lower than Best Buy. The company believed the best way to differentiate itself from the competition was to emphasize customer service by selling product warranties and offering personal services like home delivery and installation. Its purchase of Geek Squad, a 24-hour computer service company, proved profitable and strategically wise as home and small-office networks became more complex and the need for personal computing attention increased. By 2004, Best Buy had placed a Geek Squad station in each of its stores, providing consumers with personal computing services in multiple channels: in the stores, online, on the phone, and at home.

Best Buy also segmented its broad customer base into a handful of specific targets such as the affluent tech geek, the busy suburban mom, the young gadget enthusiast, and the price-conscious dad. It used extensive research to determine which segments were the most abundant and lucrative in each market and configured its stores and trained its employees to target those shoppers. For example, stores targeting affluent tech geeks offered a separate home theatre department with knowledgeable salespeople on location. Stores with a high volume of suburban mom shoppers offered personal shopping assistants to help Mom get in and out as quickly as possible with the exact items she needed.

Sometimes a store experienced a new type of lucrative customer. For example, in the coastal town of Baytown, Texas, the local Best Buy observed frequent visits from Eastern European workers coming off cargo ships and oil tankers. These men and women used their precious free time to race over to the store and search the aisles for Apple's iPods and laptops, which were cheaper in the United States than in Europe. To cater to this unique consumer, the store rearranged its layout, moving iPods, MacBooks, and their accessories from the back to the front, and added signage in simple English. The result: Sales from these European workers increased 67 percent.

Best Buy is hailed for growing into a $50 billion company virtually through one channel. However, in recent years, the company has struggled to maintain its retailing dominance. One reason is that consumers no longer have the same interest in large television sets, computers, or entertainment centers that took up so much retail space in years past. In addition, "showrooming" has become a problem, in which consumers visit stores to look, touch, and test out the products but leave empty-handed and purchase online instead. In fact, online retailers like Amazon.com have become Best Buy's biggest competitors in recent years. The company's overall market share in electronics and appliances is 16 percent, but it has only a 7 percent market share online. In comparison, Amazon's overall market share in electronics/appliances is 4 percent, but it is the market leader online, with a 21 percent market share.

Best Buy has acknowledged that it was slow to respond to category and channel shifts and was too focused on a single channel strategy when consumers' behaviors were changing. As a result, sales slipped, customer satisfaction declined, and stock value went with it. To turn things around, the company hired a new CEO who implemented a strategic initiative in 2013. "Renew Blue" was developed to reinvigorate and rejuvenate the customer experience. Online, Best Buy put a huge emphasis on improving the consumer's experience with faster and easier navigation tools, more competitive pricing, and relevant product offerings. The company also started shipping many of its online orders directly from nearby store locations, which improved delivery time and inventory turns.

Within its 1,477 domestic retail stores, Best Buy integrated a new optimization layout, which allocated additional space to growing and more profitable products like smart phones and reduced space for declining categories like entertainment. The company also plans to decrease the number of large stores it operates and increase the number of smaller, mobile stores.

As Best Buy evolves from a single-channel to a multichannel retailer, it faces many opportunities to grow its business even further. The U.S. consumer electronics and appliance market is a $228 billion industry, and the company is making changes to compete better and capture more market share. With so many storefronts across the nation, Best Buy has a competitive advantage and can leverage these assets as it expands into more channels.

Questions

1. What were the keys to Best Buy's success? What are the challenges it faces in today's retail environment?
2. How else can Best Buy compete against retail competitors like Walmart and Costco as well as online competitors like Amazon.com?

Sources: Jena McGregor, "At Best Buy, Marketing Goes Micro," *Businessweek,* May 15, 2008; Matt Richtel, "Last Man Standing," *The New York Times,* July 17, 2009; Matthew Boyle, "Best Buy's Giant Gamble," *Fortune*, March 29, 2006; Millstein, "Best Buy's Quest to Master Customer Centricity," *Chain Store Age,* December 2007; Ann Zimmerman, "Best Buy Plays Web Hardball," *Wall Street Journal*, October 12, 2012; Walter Loeb, "Best Buy in Turmoil, Will It Survive?," *Forbes,* August 22, 2012; Paula Rosenblum, "Can Best Buy Survive and Are Its Problems Really All about Amazon?," *Forbes,* August 12, 2013; Margaret Bogenrief, "Best Buy Is Pulling Off an Incredible Turnaround," *BusinessInsider,* July 30, 2013; NPD, Nielsen, Stevenson Traqline, Best Buy internal analysis, "Renew Blue," Best Buy Analyst and Investor Day presentation, November 12, 2012; BestBuy.com, 2012 Annual Report.

Part 7 Communicating Value

In This Chapter, We Will Address the Following **Questions**

1. What is the role of marketing communications? (p. 580)
2. What is the marketing communications mix? (p. 581)
3. How do marketing communications work? (p. 583)
4. What are the major steps in developing effective communications? (p. 586)
5. How should the communications mix be set and evaluated? (p. 595)
6. What is an integrated marketing communications program? (p. 599)

Oreo has become a truly global brand by creatively communicating its message of "togetherness" and "milk's favorite cookie" in markets around the world.

Source: ASSOCIATED PRESS