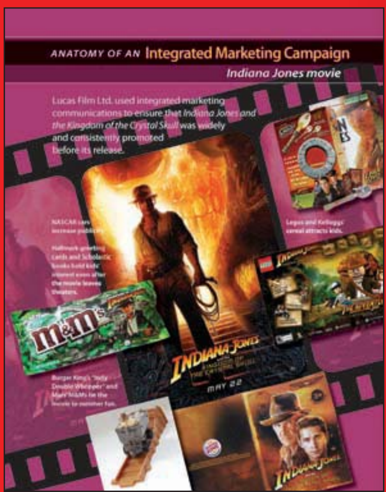
Lamb Hair McDaniel

Marketing

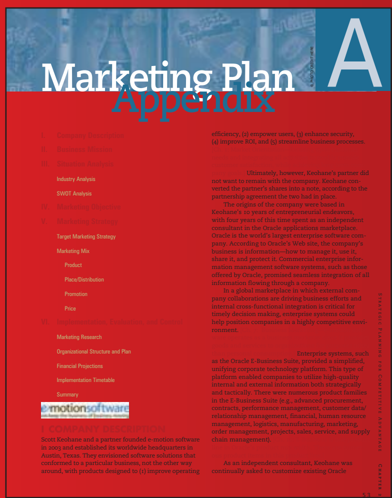
A GUIDE TO THE FEATURES

Marketing just got personal. And that's just as it should be. Nowhere is the study of marketing more personal and hands-on than *Marketing,* 10e. Completely up-to-date with today's fast-paced marketplace, *Marketing,* 10e immerses you into the dynamic field of marketing. "Anatomy of" features graphically illustrate marketing concepts. Our new Annotated Marketing Plan ties text material directly to a professional marketing plan. Intriguing statistics and short surveys make chapter topics more relevant right now, while the text's emphasis on ethics, critical thinking skills, and global issues ensures you are well-prepared for a future in marketing. Real-world examples spotlight the success stories of marketing powerhouses, but Marketing Miscues also allow you to learn from big-name mistakes. *Marketing,* 10e combines cutting-edge coverage with innovative features to help you recognize marketing in your everyday life—and learn to think like a marketer. **Now *That's* Marketing!**



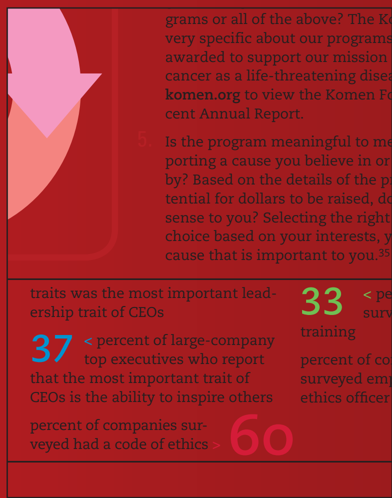
NEW! "Anatomy of" Feature

For each part in the Tenth Edition of *Marketing*, we have created a unique graphic that illustrates a particular part concept. Set on a full page, each "Anatomy of" uses photography to show how the elements of a concept connect. Highlighting a multinational company, the buying decision, packaging design, product life cycle, store layout, integrated marketing campaign, and more, "Anatomies" help you visualize the connection between marketing concepts and real-world application.



NEW! Annotated Marketing Plan

Our new marketing plan appendix after Chapter 2 includes annotations that tie each part of the plan to the material throughout the book. You'll see the correlation between chapter concepts and the elements of a professional marketing plan for a real company.



NEW! "By the Numbers" Feature

Each chapter concludes with a quick numeric recap of some of the most interesting statistics covered. "By the Numbers" keeps marketing alive and acts as an engaging and visual conclusion to the chapter.

That's Marketing!

Marketing & You Surveys

Adapted from material in the *Marketing Scales Handbook,* these brief polls are an engaging way to introduce you to a new concept. They cleverly show that you already have marketing experience—even though this may be your first course. Scoring instructions and general results are provided. Though not meant to be used in a scientific context, "Marketing & You" delivers a fun way to introduce chapter material in the context of your daily life.

Global Perspectives Boxes

Most businesses in today's market compete not only locally and nationally, but globally as well. Companies that never even considered exporting now face competition abroad. Thinking globally should be a part of every manager's tactical and strategic planning. That's why global marketing is covered in detail early on—in Chapter 5—as well as fully integrated throughout the book, cases, and videos. In addition, "Global Perspectives" boxes offer expanded examples of marketing issues facing companies on several continents—including how U.S. ethical practices compare around the globe, McDonald's move into Russia, luxury retailers as global giants, and more.

Ethics in Marketing Boxes

The Tenth Edition continues our emphasis on ethics. Completely revised and updated, intriguing "Ethics in Marketing" boxes—complete with questions focusing on ethical decision making—provide provocative examples of how ethics comes into play in many marketing decisions. You'll get personal experience grappling with hotly debated ethical questions: Is it ethical to advertise prescription drugs directly to consumers? Is it right for companies to use teens as buzz agents for their products? Are organic claims about products misleading? Are multiple distribution channels unethical?

Case Studies

One of the most powerful illustrations of how marketing concepts operate in the real world is the case study. Twelve chapters have new cases, highlighting the challenges facing marketers in the 21st century. Cases focus on a wide variety of companies, including Product Red, Starbucks China, Coke Zero, Red Lobster, Terracycle, iPhone, Nordstrom, and others.

Company Clips

The Tenth Edition retains our unique set of videos on companies you recognize—and relate to. Averaging 8 minutes, Company Clips segments cover core marketing issues facing Method, Ready-Made Magazine, Sephora, Vans, Kodak, and Acid+All. Related summaries and discussion questions are included at the end of each chapter.

Marketing Miscues

Mistakes can have tough consequences, but they also offer a great lesson. This is especially true in marketing. Helping you learn from the marketing missteps of others, new end-of-part cases describe ideas—good and bad—that couldn't make it in the rough-and-tumble marketplace. Often amusing and always interesting, these cases include such marketing gaffes as Dr Pepper using a historic cemetery as the final stop in a promotional treasure hunt, Heinz using ethnic stereotypes as names for new flavors in its Mean Beanz line of baked beans, Amazon ignoring terms of sale in its pricing and sale of video games, and more. After all, smart decision making is at the heart of successful marketing.

Critical Thinking Cases

In today's dynamic business environment, managers must constantly make decisions—meaning it's critical for marketers to be able to quickly evaluate data and craft appropriate response strategies. All new for the Tenth Edition, the comprehensive case at the end of each of the seven major parts is more challenging—ensuring you develop the critical thinking skills so essential to modern marketing. Featuring issues confronting well-known brands like Cannondale, McDonald's, and Lenovo, "Critical Thinking Cases" ask you to evaluate the situation, identify key issues, and make decisions.

Lamb Hair McDaniel

Marketing

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Marketing, 10e

Lamb, Hair, McDaniel

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To my grandkids, Cameron, Chandler, Lauren, Ashley, and Bennett.
—Charles W. Lamb

To Dale, Joe III, Kerrie and Joe IV — who all make life for me wonderful.
—Joseph F. Hair, Jr.

To Eric, Michelle, and Mimi Olson.
—Carl McDaniel

Lamb Hair McDaniel

Marketing

Tenth Edition

Brief Contents

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Preface

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ABOUT THIS EDITION

Your students experience marketing through billboards, television commercials, and even in the cereal aisle at the grocery store. *Marketing 10e* with its engaging presentation of concepts will give students the ability to recognize how much marketing principles play a role in their day to day lives. With coverage of current marketing practices and exciting new features Lamb, Hair, McDaniel's *Marketing 10e* will have your students saying, "Now *that's* marketing."

SO WHAT'S NEW?

If you are already familiar with *Marketing*, you may be asking, "So what's new?" The answer is quite a bit.

New Content

In addition to the dozens of new examples in each chapter, we have added new topical content and revised and updated existing material throughout the book.

PART 1 We have retained the proven format of Chapter 1 (An Overview of Marketing) and the Career Appendix that introduces students to various aspects of a career in marketing, like types of marketing jobs, pay scales, preparation for interviewing, and what to expect the first year on the job. Chapter 2 (Strategic Planning for Competitive Advantage) reintegrates the BCG portfolio matrix and culminates with a Marketing Plan Appendix on E-motion software, a real company based in Massachusetts. The thorough—and real—marketing plan helps students better understand the level of detail needed in plotting out a marketing strategy. Based on feedback, we've divided our old chapter on social responsibility and the marketing environment into two new chapters: Chapter 3 (Ethics and Social Responsibility). Chapter 3 covers the concept of civil society and the role ethics play in keeping it functioning smoothly. The chapter explores in depth the concepts of morality and business ethics, ethical decision making, and the cultural differences that affect the understanding and application of ethics. Chapter 3 concludes with a detailed discussion of corporate social responsibility and cause related marketing. New Chapter 4 (The Marketing Environment) offers detailed updates on demographic groups and has new material related to global innovation as a technological factor in the marketing environment. Chapter 5 (Developing a Global Vision) has been greatly revised to reflect constant changes in the global marketplace. There is new material on job outsourcing and the growing protectionist trend of blocking foreign investment. Chapter 5 also covers doing business in India and China, and a new section updates the status of the European Union and how the U.S. interacts with the E.U. as a trading partner.

PART 2 Chapter 6 (Consumer Decision Making) has been streamlined to keep the material focused. New examples keep the discussion relevant for today. Chapter 7 (Business Marketing) has new statistics on business marketing on the Internet and discussion of trends related to reintermediation. In Chapter 8 (Segmenting and Targeting Markets) we've thoroughly updated all the sections on age, gender, and ethnic segmentation with the latest data and information on trends in behavior. The section on perceptual mapping has been updated with new graphics. Chapter 9 (Decision Support Systems and Marketing Research) has an new expanded example to illustrate the research process The sections on mystery shopping and ethnographic research have been updated and expanded. The section on blogging has been reframed to include the larger category of consumer-generated media and how marketers make use of such media in their research efforts. A new section on how companies are using behavioral targeting combined with marketing research to increase advertising response and sales.

PART 3 Chapter 10 (Product Concepts) has been refreshed with new examples, and Chapter 11 (Developing and Managing Products) has a completely updated section on the importance of innovation and revised material on the marketing implications of the diffusion process. Chapter 12 (Services and Nonprofit Organization Marketing) uses new examples to illustrate the Gap model and introduces the concept of peer-to-peer communication as a promotional tool used by nonprofit organizations.

PART 4 In many ways, business success depends on the efficiency and effectiveness of a company's supply chain. That's why for the Tenth Edition, we have divided our old chapter on channels and supply chains into two new chapters to give each of these topics coverage that reflects their critical nature to today's marketers. Chapter 13 (Marketing Channels) identifies channel members and their functions, describes channel structures, discusses how managers make channel strategy decisions, and explains the types of channel relationships and how they are managed. Chapter 14 (Supply Chain Management) introduces supply chain integration in a detailed section that precedes the discussion of the key processes of supply chain management, including CRM, CSM, demand management, order fulfillment, manufacturing flow, supplier relationships, product development, and returns management. Chapter 14 also covers the logistics function in the supply chain and identifies the ways companies assess the performance of the their supply chains. Chapter 15 (Retailing) contains new trends like pop-up shops and store-in-a-store that are becoming more prevalent and includes new information on the impact location decisions on stores. The chapter also includes updated retailing statistics.

PART 5. Chapter 16 (Promotional Planning for Competitive Advantage) has been thoroughly revised and reorganized to reflect the format followed in Chapter 2 on marketing strategy. The communication process is described in detail, a quick introduction to the promotional mix follows before a more thorough discussion of promotional goals, AIDA, and integrated marketing communication is given. The chapter also includes information on the factors affecting the promotional mix as well as new examples throughout to keep the chapter content relevant for today's students. Chapter 17 (Advertising and Public Relations) stays abreast of a wide variety of alternative media, including social media marketing. Current statistics on the impact of advertising and internet advertising keep the chapter up to date. Chapter 18 (Sales Promotion and Personal Selling) has been streamlined to keep students focused on the high-level issues related to sales promotion and personal selling.

PART 6 Chapter 19 (Pricing Concepts) includes a revised section on pricing power. The chapter also includes new sections on targeting technology used in conjunction with yield management systems and on guaranteed price matching. Revised legislation on resale price maintenance and predatory bidding is covered in Chapter 20 (Setting the Right Price), illustrating the dynamic impact of the legal environment on pricing decisions. The section on discounts now includes an explanation of *markdown money*, and the strategy of making strong promotional claims and avoiding discounting is now part of the discussion on demand-oriented pricing tactics used during periods of inflation. Chapter 20 also covers the latest cases in price fixing.

PART 7 You may be wondering what we've done with the Internet chapter. Because the Internet touches every aspect of marketing, we have moved the content from that chapter into relevant chapters throughout the book. You'll read integrated Internet content in every chapter. New examples help illustrate the complex topic of Customer Relationship Management the subject of Chapter 21.

New "Anatomy of" Feature

For several chapters in the Tenth Edition of *Marketing*, we have created a unique graphic that illustrates a particular chapter concept. Each "Ánatomy of" is set on full page and uses photography to show how the elements of a concept connect. The Tenth Edition includes anatomies of a multinational company, buying decision, packaging design, product life cycle, store layout, integrated marketing campaign, and more. Anatomies help students visualize the connection between marketing concepts and their real-world application.

New Annotated Marketing Plan

Our new marketing plan appendix after Chapter 2 includes annotations that tie each part of the plan to the material throughout the book Students will see the correlation between the chapters in the book and the elements of a professional marketing plan for a real company.

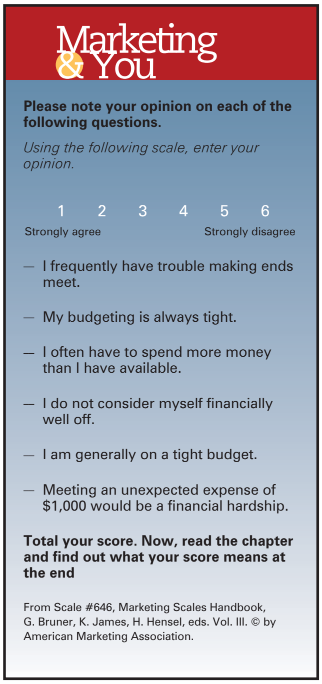
New "By the Numbers" Feature

Each chapter concludes with a quick numeric recap of the some of the interesting statistics from the chapter. By the Numbers keeps marketing alive for students and acts as an engaging and visual conclusion to the chapter.

CLASSIC FEATURES HAVE BEEN UPDATED AND ENHANCED

Marketing and You Surveys

Today's students demand their courses be relevant, and to help you make that connection, we have added a short survey to each chapter opener. Adapted from material in the *Marketing Scales Handbook*, these short polls are an engaging way to introduce students to a new concept. Even though this is their first marketing course, Marketing & You polls show them that they


Marketing & You

Please note your opinion on each of the following questions.

Using the following scale, enter your opinion.

1 2 3 4 5 6
Strongly agree — Strongly disagree

— I frequently have trouble making ends meet.

— My budgeting is always tight.

— I often have to spend more money than I have available.

— I do not consider myself financially well off.

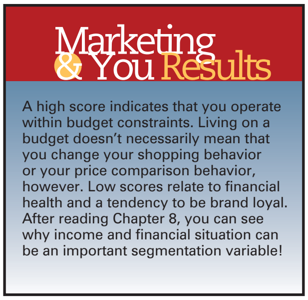
— I am generally on a tight budget.

— Meeting an unexpected expense of $1,000 would be a financial hardship.

Total your score. Now, read the chapter and find out what your score means at the end

From Scale #646, Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds. Vol. III. © by American Marketing Association.

already have experience with marketing. Scoring instructions are given, and general results provided. Marketing & You is *not* meant to be used in a scientific context; it is just an interesting and fun way to introduce the chapter material.

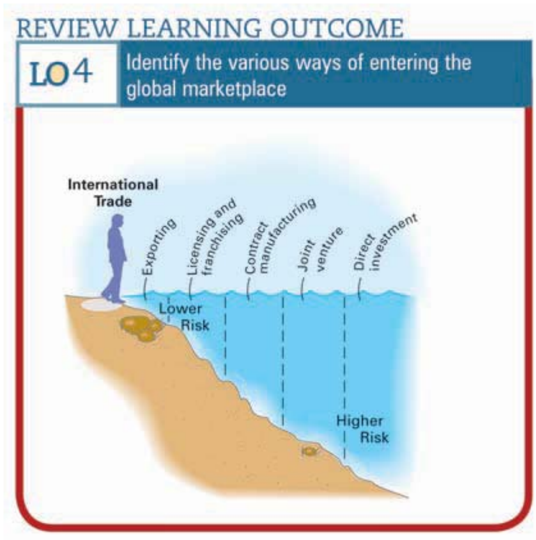

Marketing & You Results

A high score indicates that you operate within budget constraints. Living on a budget doesn't necessarily mean that you change your shopping behavior or your price comparison behavior, however. Low scores relate to financial health and a tendency to be brand loyal. After reading Chapter 8, you can see why income and financial situation can be an important segmentation variable!

Visual Learning Outcome Summaries

Through our years of teaching, we know that not all students learn the material the same way. Some can read books and understand the concepts just from their verbal presentation. Other students need to rewrite the material in their own words in order to understand it completely. Still others learn best from diagrams and exhibits. Student focus groups have confirmed this experience in a more quantitative way.

For this reason, we have retained our visual **Review Learning Outcomes,** which are designed to give students a picture of the content, to help them recall the material. For example, Learning Outcome 4 in Chapter 5 discusses the various ways of entering the global marketing place. The detailed discussion, of everything from exporting to direct investment, ends with the following review:



These reviews are not meant to repeat every nuance of the chapter content. Rather, they are meant to provide visual cues that prompt the student to recall the salient points in the chapter.

Global Perspectives Boxes

Today most businesses compete not only locally and nationally, but globally as well. Companies that may have never given a thought to exporting now face competition abroad. Thinking globally should be a part of every manager's tactical and strategic planning. Accordingly, we address this topic in detail early in Chapter 5. Global marketing is fully integrated throughout the book, cases, and videos, as well.

Our **Global Perspectives** boxes provide expanded global examples of the marketing issues facing companies on several continents. Each box concludes with thought-provoking questions carefully prepared to stimulate class discussion. You'll read about how U.S. ethical practices compare around the globe, McDonald's is moving into Russia, luxury retailers are becoming global giants, and more.


GLOBAL Perspectives

McDONALD'S IN RUSSIA

GLOBAL

Of the 118 countries where McDonald's Corp. does business, none can boast more activity than Russia. On average, each location serves about 850,000 diners annually—more than twice the average individual store traffic in most other markets McDonald's serves.

This has presented the world's largest restaurant chain with an unusual dilemma. Russia, with its burgeoning middle class and consumer appetites for all things American, is a jewel in the McDonald's system. But the company is being prudent about expansion here—due partly to Russia's famous bureaucracy and partly to the chain's own philosophical shift.

Aggressive growth plans at McDonald's have backfired badly in the past. During the 1990s, the company was fixated on adding restaurants throughout the chain—as many as 2,500 stores a year. But by 2000, the condition of its existing locations, as well as the appeal of certain menu items, deteriorated. Two years later, the company's flawed expansion strategy was hammering its profits and stock price.

Aiming then to be "better, not just bigger," the Oak Brook, Ill., company reined in expansion. In 2003, when McDonald's reported its first-ever quarterly loss, it opened a net of 21 new stores—down from 1,015 in the previous year.

New emphasis was placed on improving signature products such as the Big Mac and Chicken McNuggets. Executives also called for an aesthetic overhaul, using more muted colors and lighting schemes in the stores. The changes helped lift sales and profits, ushering in one of the company's most successful performance streaks to date. McDonald's share rose by 33 percent in the year following these changes.

In Russia, the company is now working to squeeze more sales and profits from its 180 existing locations rather than over-rely on new restaurants. To do so, Khamzat Khasbulatov, chief executive of McDonald's Russia, is taking a page from Western-style dining habits. He has introduced a breakfast menu and plans to add more "McCafé" sections serving espresso drinks to draw late afternoon and evening crowds. He is also trying to increase the number of restaurants that have drive-throughs and twenty-four hour service. "You have to keep your restaurants relevant to your consumer," he says. Mr. Khasbulatov is also focusing on ways to move lines and customer traffic more quickly. In some locations, employees take orders on handheld devices before customers reach the counter. Special cooking equipment also hastens the diner's experience. A new toaster, for instance, browns sandwich buns in 14 seconds, less than half what it used to take, according to Karina Pogosova, junior vice president of operations for McDonald's Russia.

Mr. Khasbulatov doesn't want the lines to disappear entirely. "When I said I have too many customers, it's a nice problem to have," he says. "I would love to continue to have this problem."[16]

What marketing management philosophy does McDonald's in Russia appear to be following? Explain.

7 AN OVERVIEW OF MARKETING CHAPTER 1

Ethics in Marketing Boxes

In this edition we continue our emphasis on ethics. The **Ethics in Marketing** boxes, complete with questions focusing on ethical decision making, have all been revised. This feature offers provocative examples of how ethics comes into play in many marketing decisions. Is it ethical to advertise prescription drugs direct to consumers? Is it right for companies to use teens as buzz agents for their products? Are organic claims about products misleading? Are multiple distribution channels unethical? Students will consider these and many other hotly debated, ethical questions.

ETHICS in Marketing

Targeting Kids 8-and-under

Marketers have long advertised their products to adolescents, tweens and grade-schoolers. However, three quarters of U.S. children watching ads for toys, athletic shoes, and snack food each day are under 6 years old, and 43 percent are younger than 2. According the American Psychological Association, the concept of a "commercial" means nothing to children under age 9. They perceive ad claims facts because they can't understand the motives and persuasive intent behind commercials.

Some marketers argue that they are targeting their parents, not the kids themselves. For example, Josef Mandelbaum, president of American Greetings Intellectual Properties, owner of Care Bears and Strawberry Shortcake, claims that television shows based on these characters reinforce the brands to kids, but don't target them with advertising. Others such as Disney, McDonald's, and Hasbro openly admit that 5- and 6-year-old children are a reasonable target for their products. Kids even get a dose of advertising-related messages before and at school. The trip to school may include Bus Radio with ads from companies such as News Corp., Disney, Cartoon Network, and AT&T. Corporate sponsor logos, branded vending machines, and book covers sponsored by PepsiCo, Hasbro, and Ronald McDonald can be found on school grounds.

Research confirms that kids are learning to be consumers early in life. A study by the Campaign for a Commercial-Free Childhood (CCFC) found that children between 4 and 12 years old spent $30 billion in 2002, up from $6.1 billion in 1989. And, according to another study, kids influence another $600 billion a year in family spending. One third of kids between 4 and 6 years old have their own DVD player, a handheld videogame player, and a television set in their rooms. Ninety percent of these children use some form of screen media every day for an average of two hours. Thus, kids form a large target market, and they are easy for companies to reach with advertising and product-related messages.

Marketers are spending $15 billion a year to reach young children, who now see roughly 40,000 television commercials each year. Other marketing activities range from creation of the McDonald's Happy Meal to interactive activities kids can find online. For example, Pepperidge Farm offers "Goldfish Central," a Web site where "Finn," a spokes-fish for the fish-shaped snack food, invites kids into a virtual world of adventures featuring his many fish friends.

CCFC and other advocacy groups have taken the position that there is no moral, ethical or social justification for advertising to children. The issue is not only the presence of kid-focused advertising but also of brand integration into entertainment, linking kids' movies and snack foods, and product peddling by licensed characters. The solution the advocacy groups support is not regulation, but a total ban on kid marketing, like that in many European countries.

On the other side, marketers claim that it would be nearly impossible to ensure that kids don't view advertising given the proliferation of media. Some marketers argue that parents should act as filters for media content and educate their children about ads. Others claim that advertising to children under 8 can be done responsibly. Julie Halpin, CEO of the Geppetto Group, a New-York based marketing firm that works with companies such as Coca Cola, Reebok and Unilever, maintains that they serve the client's business objectives and the best interests of kids. Some companies have taken measures to be responsible advertisers to kids. Fisher Price, which aims about 20 percent of its ads to children as young as 3 or 4, tests its marketing on focus groups of kids and parents, using the latter's input to guide content and approach.

Is it acceptable for marketers to target young children with advertising messages? If so, what should the content and approach of these messages be? If not, how would you implement regulations or a ban on kid marketing?

SOURCE: Based on T. L. Stanley, "Babes in Brandland," *Brandweek*, October 15, 2007, 29-30.

Exercises

APPLICATION EXERCISE

Purchasing agents are often offered gifts and gratuities. Increasingly, though, companies are restricting the amount and value of gifts that their purchasing managers can accept from vendors. The idea is that purchasing managers should consider all qualified vendors during a buying decision instead of only those who pass out great event tickets. This exercise asks you to consider whether accepting various types of gifts is ethical.[25]

Activities

1. Review the following list of common types of gifts and favors. Put a checkmark next to the items that you think it would be acceptable for a purchasing manager to receive from a vendor.
   —Advertising souvenirs
   —Clothing
   —Discounts on personal purchases
   —Golf outings
   —Large appliances
   —Lunches
   —Tickets (sports, theater, amusement parks, etc.)
   —Vacation trips
   —Automobiles
   —Dinners
   —Food and liquor
   —Holiday gifts
   —Loans of money
   —Small-value appliances
   —Trips to vendor plants
2. Now look at your list of acceptable gifts through various lenses. Would your list change if the purchasing manager's buying decision involved a low-cost item (say, pens)? Why or why not? What if the decision involved a very expensive purchase (like a major installation)?
3. Form a team and compare your lists. Discuss (or debate) any discrepancies.

227 Business Marketing Chapter 7

Review and Applications

To help students focus their study time, we continue to group end-of-chapter discussions and writing questions with their related learning outcome summary. Questions are numbered according to the learning outcome to which they correspond. For example, the summary point for Chapter 12, Learning Outcome 5 has three related questions. They are numbered 5.1, 5.2, and 5.3. This organization helps students identify questions pertinent to the learning outcome they are studying, allowing each chapter to function as a series of content blocks that can be read over multiple study sessions.

LO 5 Discuss relationship marketing in services. Relationship marketing in services involves attracting, developing, and retaining customer relationships. There are three levels of relationship marketing: level 1 focuses on pricing incentives; level 2 uses pricing incentives and social bonds with customers; and level 3 uses pricing, social bonds, and structural bonds to build long-term relationships.

TEAM

5.1 For the new service developed for question 4.1, have the members of the team discuss how they would implement a relationship marketing strategy.

Application Exercises

Application exercises at the end of each chapter give students the opportunity to work with marketing concepts in various real-world contexts. We incorporate activities (rather than questions) to help students appreciate the width and depth of the marketing industry. These exercises come from instructors around the country who have contributed their teaching ideas to our unique supplement, **Great Ideas in Teaching Marketing,** since the First Edition. Each exercise selected was a winner in the "Best of the Great Ideas in Teaching Marketing," as voted by a panel of 35 faculty judges. You can be sure that these applications will be successful whether used as classroom activities or team projects assignments.

Some examples are researching the complete supply chain for a specified product; creating an advertising campaign for a product, using the rules from the Hasbro game Taboo; role playing a televised interview after a marketing crisis; and much more.

Ethics Exercise

The business press has reported on numerous scandals and trials in recent years. Although some might say that these occurrences are the work of a few bad apples spoiling the bunch, it is clear that ethical decision making plays a very important role in a company's success and prosperity. An **Ethics Exercise** appears at the end of every chapter. A brief scenario presents students with a situation in which the right thing to do may or may not be crystal clear. Use these exercises to show students the limitations to a code of ethics and to reinforce the importance of not simply consulting existing rules of conduct, but also of developing an ethical personality.

ETHICS EXERCISE

Abercrombie & Fitch, a retail clothing chain based in New Albany, Ohio, launched a line of thong underwear for preteen girls. Words like "eye candy" and "wink wink" were printed on the front of the skimpy underwear that some argued would fit girls aged 5 to 10. Abercrombie is known for its provocative ads and sexually oriented catalogs. Supporters of the strategy claim that producing thong-style underwear for 10- to 16-year olds is a good move; critics think that the line is tasteless and that marketing it to young girls is contemptuous.

Questions

1. Is marketing adult-styled undergarments to a younger audience unethical? Why or why not?
2. Would Abercrombie have been in the spotlight had the sexy words been omitted from the product? Explain your answer.

Case Studies

One of the most powerful illustrations of how marketing concepts operate in the real world is the case study. Twelve chapters have new entrepreneurship cases, highlighting the challenges facing entrepreneurs in the 21st century. These cases focus on a wide variety of companies, like Product Red, Starbucks China, Coke Zero, Red Lobster, Terracycle, iPhone, Nordstrom, and others. Your students will find these cases an exciting and challenging aspect of each chapter.

Case Study: Product (Red)

© SUSAN VAN ETTEN

CAN A T-SHIRT SAVE THE WORLD?[37]

When Oprah and Bono walked down Chicago's Magnificent Mile together in the fall of 2006, it was the shopping trip seen around the world. The famous duo attracted mobs of fans and extensive media coverage as they promoted a revolutionary new cause-marketing event called (Product) RED. Bono urged people to buy RED products, explaining that a portion of the proceeds would go to The Global Fund to fight HIV/AIDS in Africa. Oprah, wearing an "INSPI(RED)" Gap t-shirt on her talk show that day, proclaimed, "I am wearing the most important t-shirt I've ever worn in my life!"

Other companies that licensed the RED brand and created products for the charity included Apple, which sold a limited edition iPod nano, and Motorola, which introduced a red Motorazr phone. Emporio Armani designed a special RED capsule collection for London Fashion Week, and Converse designed a line of RED shoes to be sold at Gap stores.

Company Clips

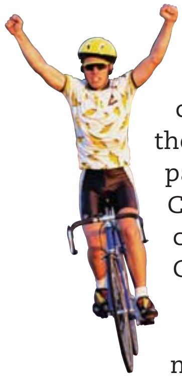
The Tenth Edition retains our unique set of videos on companies your students and you will recognize, as well as the related summaries and discussion questions at the end of each chapter. Company Clips segments average 8 minutes in length, which is enough time to cover core marketing issues facing Method, ReadyMade Magazine, Sephora, Vans, Kodak, and Acid+All. Segments are rich enough to allow you to teach through the video, integrating lecture and video to create a richer learning experience. Tips on how to do this are included in the Instructor Manual with Video Guide.

Marketing Miscues

Mistakes can have tough consequences, but they also offer a great lesson. This is especially true in marketing. At the end of each part, you will find new cases that describe good and bad ideas that couldn't make it in the rough-and-tumble marketplace. Often amusing and always interesting, these cases, including Dr. Pepper using an historic cemetery as the final stop in a promotional treasure hunt, Heinz using ethnic stereotypes as names for new flavors in its Mean Beanz line of baked beans, Amazon ignoring terms of sale in its pricing and sale of video games, will help your students avoid the same mistakes made by these well-known companies. After all, making smart decisions is at the heart of successful marketing.

Critical Thinking Cases

In today's dynamic business environment, managers must constantly make decisions. For that reason, marketers must be able to quickly evaluate data and craft appropriate response strategies. In the hope of better preparing the next generation of business leaders, *Marketing*, Tenth Edition, helps students develop critical thinking skills with a more challenging comprehensive case at the end of each of the seven major parts—all of them new for this edition. Critical Thinking Cases feature issues confronting well-known brands like Cannondale, McDonald's, and Lenovo, and ask students to evaluate the situation, identify key issues, and make decisions.



OUR PEDAGOGY IS DESIGNED WITH YOUR STUDENTS IN MIND

All of our content is anchored by the cornerstone of our text, our fully **Integrated Learning System (ILS).** The text and all major supplements are organized around the learning outcomes that appear at the beginning of each chapter, so *Marketing* is both easy to teach from and to learn.

Just like the content in the textbook, material in the Instructor Manual, Test Bank, and PowerPoint presentation is all clearly organized by learning outcome number. In addition, we consider multiple learning styles in the organization of our text pedagogy.

Our Text Pedagogy Excites and Reinforces Learning

Pedagogical features are meant to reinforce learning, but that doesn't mean that they have to be boring. We have created teaching tools within the text itself that will excite student interest as well as teach. Not one of our features is casually included: each has been designed and written to meet a specific learning need, level, or style.

- **Terms:** Key terms appear in boldface in the text, with definitions in the margins, making it easy for students to check their understanding of key definitions. A complete alphabetical list of key terms appears at the end of each chapter as a study checklist, with page citations for easy reference.
- **Review and Applications:** The end of each chapter contains a section titled Review and Applications, a summary that distills the main points of the chapter. Chapter summaries are organized around the learning outcomes so that students can quickly check their understanding of chapter concepts. Discussion questions and activities are under the learning outcome to which they pertain.
- **Writing Questions:** To help students improve their writing skills, we have included writing exercises in the review section at the end of each chapter. These

WRITING

exercises are marked with the icon shown here. The writing questions are designed to be brief, so that students can accomplish writing assignments in a short time and instructors' grading time is minimized.

- **Team Activities:** The ability to work collaboratively is a key to success in today's business world. End-of-chapter team activities, identified by the icon shown here, give students opportunities to learn to work together by engaging in consensus building and problem solving.
- **Online Activities:** Understanding how to use the Internet for professional (and academic) purposes is critical in today's business environment. End-of-chapter activities accompanied by the icon to the left give the students the opportunity to hone their skills in this area.
- **Application Exercise:** These activities are based on winning teaching ideas from the "Best of the Great Ideas in Teaching Marketing" contest held in conjunction with the publication of the Eighth Edition. Developed by professors across the country, these exercises allow students to explore the principles of marketing in greater detail through engaging and enjoyable activities.
- **Ethics Exercise:** Short ethical dilemmas help students practice doing the right thing. Questions following each scenario prompt students to make an ethical decision and explain the rationale behind it.
- **Case Studies:** All chapters contain case study with questions that help students work through problems facing real small businesses today.
- **Company Clips:** All chapters contain a summary of the Company Clip video with related viewing and discussion questions.

All components of our comprehensive support package have been developed to help you prepare lectures and tests as quickly and easily as possible. We provide a wealth of information and activities beyond the text to supplement your lectures, as well as teaching aids in a variety of formats to fit your own teaching style.

WE INTEGRATE TECHNOLOGY IN A MEANINGFUL WAY

From the beginning, we have integrated new technologies into our Integrated Learning System in a meaningful way. The Tenth Edition continues this tradition by adding new and exciting content to our technology materials. We have also enhanced and refined popular media supplements to bring concepts alive in the classroom.

Web Tutor™ (for both WebCT®, and Blackboard®)

Online learning is growing at a rapid pace. Whether you are looking to offer courses at distance or to offer a Web-enhanced classroom, South-Western/Cengage Learning offers you a solution with WebTutor. WebTutor provides instructors with text-specific content that interacts with the two leading systems of higher education course management–WebCT and Blackboard.

WebTutor is a turnkey solution for instructors who want to begin using technology like Blackboard or WebCT but who do not have Web-ready content available, or who do not want to be burdened with developing their own content. WebTutor uses the Internet to turn everyone in your class into a front-row student. WebTutor offers interactive study guide features such as quizzes, concept reviews, animated figures, flashcards, discussion forums, Ask the Author and Company Clip video clips, and more. Instructor tools are also provided to facilitate communication between students and faculty.

Who Wants to Be a Marketer?

When we debuted **Who Wants to Be a Marketer?** with the Sixth Edition, we did not anticipate how popular it would become. Developed by John Drea of Western Illinois University, this exciting supplement to the Tenth Edition of *Marketing* by Lamb, Hair, and McDaniel is an in-class, computer-based game. Who Wants to Be a Marketer? is a fun and exciting way to review terminology and concepts with students.

The game is simple to use in a traditional or an electronic classroom Formatted for Microsoft PowerPoint, the game has two rounds of fifty original questions per chapter, for a total of 1,500 questions! Both versions of Who Wants to Be a Marketer? are available only for adopters of *Marketing* by Lamb, Hair, and McDaniel.

We Offer a Companion Web Site

Lamb, Hair, and McDaniel's Web site at **www.cengage.com/marketing/lamb** contains the key supplements that support the textbook: Instructor's Manual, Test Bank, and the PowerPoint presentation without embedded video. There is also a "Talk to the Author" button where you can submit your comments and questions. For students, the companion Web site offers crossword puzzles of key terms, interactive quizzes, and career exercises with electronic resources to help them investigate careers in the various marketing fields.

INNOVATIVE AND VALUABLE INSTRUCTOR SUPPLEMENTS

Instructor Resource CD-ROM

Managing your classroom resources is now easier than ever. The new Instructor Resource CD-ROM contains all key instructor supplements—Instructor's Manual, Certified Test Bank, and PowerPoint, with embedded videos, Who Wants to Be a Marketer?, and ExamView testing software.

Video Package

Available on DVD, the video package to accompany *Marketing, 10e,* continues to showcase the nuts and bolts of marketing at modern companies. The rich Company Clip videos will help reinforce what you've learned by showing people who are doing marketing every day—and not according to thematic units.

A Value-Added Instructor Manual Like No Other

Our Instructor's Manual is the core of our **Integrated Learning System.** For the Tenth Edition of *Marketing,* we have made our popular Instructor's Manual even more valuable for new and experienced instructors alike. Here is a list of the features that will reduce class preparation time:

- Suggested syllabi for 12- and 16-week terms.
- A pedagogy grid for each chapter briefly laying out 1) all the options the professor has in the chapter, and 2) the key points addressed by the features in each chapter. The features included on the grid are the boxed features, Application Exercise, Ethics Exercise, Case Study, and Company Clip.
- Three suggested lesson plans for each chapter: a lecture lesson plan, a small-group work lesson plan, and a video lesson plan.

We have retained the proven features like the chapter outline, lists of support material, additional class activities, and solutions for all Review and Applications, Case Studies, Marketing Miscues, and Critical Thinking Cases in the book. There are also teaching tips for setting up each of the Application Exercises. Our manual is truly "one-stop shopping" for instructors teaching any size marketing course.

Certified Test Bank and Windows Testing Software

The Test Bank of the Tenth Edition has been reviewed by a panel of marketing faculty across the country who helped identify questions that may cause problems in their implementation. Faculty reviewers have helped us cull any troublesome questions. You can be sure that, no matter which questions you select for quizzes, tests, and exams, they are of the best quality. The Test Bank is organized around the learning outcomes to help you prepare on a class-by-class basis; and all questions are tagged with relevant AACSB standards to help you monitor trends in student performance necessary for accreditation. The Test Bank is available in print and new Windows software formats (ExamView testing software).

With ExamView, you can choose to prepare tests that cover all learning outcomes or that emphasize only those you feel are most important. This updated Test Bank is one of the most comprehensive on the market, with over 3,500 true/false, multiple-choice, scenario, and essay questions. Our testing database, combined with the ease of ExamView, takes the pain out of exam preparation.

WebTutor™ ToolBox

Preloaded with content and available via a free access code when packaged with this text, WebTutor™ ToolBox pairs a range of supplemental content with sophisticated course management functionality. You can assign materials (including online quizzes) and have the results flow automatically to your grade book. WebTutor™ ToolBox is ready to use as soon as you log on—or you can customize its preloaded content by uploading images and other resources, adding Web links, or creating your own practice materials. Students only have access to student resources on the Web site. Instructors can enter an access code for password-protected Instructor Resources.

Other Outstanding Supplements

- **Handbook for New Instructors: Getting Started with Great Ideas:** This helpful supplement was specifically designed for instructors preparing to teach their first course in principles of marketing. We have bolstered our helpful hints on everything from developing a course outline to grading, with winning general teachings from our "Best of the Great Ideas in Teaching Marketing" contest. To give you a complete resource for teaching ideas, we have included all of the winning entries, nearly one hundred in all, at the end of the Handbook. You'll find great teaching ideas for every chapter, plus a wealth of general tips. If you're new, let professors from around the country help you get started teaching principles of marketing!
- **Great Ideas in Teaching Marketing:** We have begun collecting Great Ideas on our instructor's resource page on the Lamb, Hair, and McDaniel Web site. In this way, we can accept submissions year-round. Great Ideas in Teaching Marketing will

still be published with each new edition of **Marketing** as part of the **Handbook for New Instructors**. You can also review all current great ideas by chapter at **www.cengage.com/marketing/lamb.**

INNOVATIVE AND VALUABLE STUDENT SUPPLEMENTS

Marketing, 10e, provides an excellent vehicle for learning the fundamentals. For students to gain a true understanding of marketing, however, it's best if they can apply the principles they are learning in the classroom. And it's best if they have study aids that address their particular learning style. Our student supplements meet the needs of a variety of learning styles, from visual to auditory, from hands-on to abstract conceptualization.

Web Tutor™ (for both WebCT®, and Blackboard®):

Students how learn best with online technology will appreciate all WebTutor has to offer their study program. From quizzes to games and threaded discussion to concept reviews, Web Tutor provides students a full range or learning tools to master principles of marketing.

Wall Street Journal Edition:

This *Wall Street Journal* edition makes it easy to bring the real world into the classroom, providing numerous opportunities to relate economic concepts to daily news stories. New copies of ***Marketing, 10e*** can include an optional card entitling students to subscriptions to the *Wall Street Journal* and WSJ.com, giving students access to many articles used as examples in this textbook. Contact your local representative pricing and optional bundling information.

MEET THE AUTHORS

Charles W. Lamb

Charles W. Lamb is the M.J. Neeley Professor of Marketing, M.J. Neeley School of Business, Texas Christian University. He served as chair of the department of marketing from 1982 to 1988 and again from 1997 to 2003. He is currently chair of the Department of Information Systems and Supply Chain Management and president of the Academy of Marketing Science.

Lamb has authored and co-authored more than a dozen books and anthologies on marketing topics and over 150 articles that have appeared in academic journals and conference proceedings.

In 1997, he was awarded the prestigious Chancellor's Award for Distinguished Research and Creative Activity at TCU. This is the highest honor that the university bestows on its faculty. Other key honors he has received include the M.J. Neeley School of Business Research Award and selection as a Distinguished Fellow of the Academy of Marketing Science and a Fellow of the Southwestern Marketing Association.

Lamb earned an associate degree from Sinclair Community College, a bachelor's degree from Miami University, an MBA from Wright State University, and a doctorate from Kent State University. He previously served as assistant and associate professor of marketing at Texas A&M University.

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Joseph Hair is Professor of Marketing at Kennesaw State University. Before that, he was the Alvin C. Copeland Endowed Chair of Franchising and Director, Entrepreneurship Institute, Louisiana State University. Before that, Hair held the Phil B. Hardin Chair of Marketing at the University of Mississippi. He has taught graduate and undergraduate marketing and marketing research courses.

Hair has authored 30 books, monographs, and cases, and over 60 articles in scholarly journals. He has also participated on many university committees and has chaired numerous departmental task forces. He serves on the editorial review boards of several journals.

He is a member of the American Marketing Association, Academy of Marketing Science, Southern Marketing Association, and Southwestern Marketing Association. He was the 2004 recipient of the Academy of Marketing Science Excellence in Teaching Award.

Hair holds a bachelor's degree in economics, a master's degree in marketing, and a doctorate in marketing, all from the University of Florida. He also serves as a marketing consultant to businesses in a variety of industries, ranging from food and retail, to financial services, health care, electronics, and the U.S. Departments of Agriculture and Interior.

Carl McDaniel

Carl McDaniel is a professor of marketing retired from the University of Texas–Arlington, where he was the chairman f the marketing department for 22 years. McDaniel's career spanned more than than 25 years during which he the recipient of several awards for outstanding teaching. McDaniel has also been a district sales manager for Southwestern Bell Telephone Company. Currently, he serves as a board member of the North Texas Higher Education Authority, a billion-dollar financial institution.

In addition to *Marketing*, McDaniel has co-authored numerous textbooks in marketing and business. McDaniel's research has appeared in such publications as the *Journal of Marketing*, *Journal of Business Research*, *Journal of the Academy of Marketing Science*, and *California Management Review*.

McDaniel is a member of the American Marketing Association, the Academy of Marketing Science, and the Society for Marketing Advances. In addition to his academic experience, McDaniel has business experience as the co-owner of a marketing research firm. Recently, McDaniel served as senior consultant to the International Trade Centre (ITC), Geneva, Switzerland. The ITC's mission is to help developing nations increase their exports. He has a bachelor's degree from the University of Arkansas and his master's degree and doctorate from Arizona State University.


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PART 1

The World of Marketing

WHAT'S INSIDE

An Overview of Marketing

CHAPTER

1

Learning Outcomes

LO 1 Define the term *marketing*

LO 2 Describe four marketing management philosophies

LO 3 Discuss the differences between sales and market orientations

LO 4 Describe several reasons for studying marketing

LO 1

What Is Marketing?

marketing
The activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large.

exchange
People giving up something to receive something they would rather have.

What does the term *marketing* mean to you? Many people think it means the same as personal selling. Others think marketing is the same as personal selling and advertising. Still others believe marketing has something to do with making products available in stores, arranging displays, and maintaining inventories of products for future sales. Actually, marketing includes all of these activities and more.

Marketing has two facets. First, it is a philosophy, an attitude, a perspective, or a management orientation that stresses customer satisfaction. Second, marketing is activities and processes used to implement this philosophy.

The American Marketing Association's definition of marketing focuses on the second facet. Marketing is the activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large.[1]

Marketing involves more than just activities performed by a group of people in a defined area or department. In the often-quoted words of David Packard, cofounder of Hewlett-Packard, "marketing is too important to be left only to the marketing department." Marketing entails processes that focus on delivering value and benefits to customers, not just selling goods, services, and/or ideas. It uses communication, distribution, and pricing strategies to provide customers and other stakeholders with the goods, services, ideas, values, and benefits they desire when and where they want them. It involves building long-term, mutually rewarding relationships when these benefit all parties concerned. Marketing also entails an understanding that organizations have many connected stakeholder "partners," including employees, suppliers, stockholders, distributors, and society at large.

Research shows that a company's ability to motivate its employees translates directly to customer satisfaction and thus to the bottom line.[2] At The Container Store, sales representatives receive 241 hours of training compared to an industry average of eight hours. The company offers health care coverage to part-time workers, and arranges schedules to allow parents to drop off and pick up their children. The Container Store has experienced 15 percent to 20 percent annual sales growth since its founding, due in part to putting employees before customers.[3] The motto of Wegmans Food Markets, the Rochester-based grocery chain ranked by *Fortune* magazine as the best company to work for in America, states, "Employees first, customers second." The rationale is that if employees are happy, customers will be too.[4]

One desired outcome of marketing is an exchange; people giving up something to receive something they would rather have. Normally, we think of money as the medium of exchange. We "give up" money to

Marketing & You

Please note your opinion on each of the following questions.

Think about where you buy cosmetics or personal care products. Using the following scale, enter the number that indicates how likely you are to:

1	2	3	4	5	6
Not likely at all					Extremely likely

— Say positive things about the company to other people.

— Recommend the company to someone who seeks your advice.

— Encourage friends and relatives to do business with the company.

— Consider the company your first choice to buy cosmetics or personal care products.

— Do more business with the company in the next few years.

Now, total your score. Read the chapter to find out what your score means at the end.

"get" the goods and services we want. Exchange does not require money, however. Two persons may barter or trade such items as baseball cards or oil paintings.

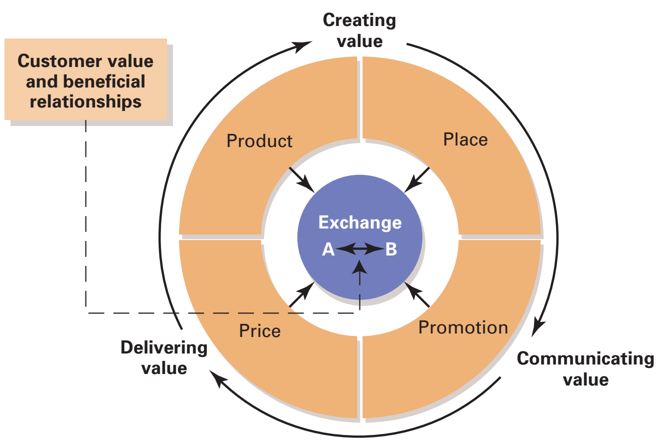
An exchange can take place only if the following five conditions exist:

1. There must be at least two parties.
2. Each party has something that might be of value to the other party.
3. Each party is capable of communication and delivery.
4. Each party is free to accept or reject the exchange offer.
5. Each party believes it is appropriate or desirable to deal with the other party.[5]

Exchange will not necessarily take place even if all these conditions exist. They are, however, necessary for exchange to be possible. For example, you may place an advertisement in your local newspaper stating that your used automobile is for sale at a certain price. Several people may call you to ask about the car, some may test-drive it, and one or more may even make you an offer. All five conditions are necessary for an exchange to exist. But unless you reach an agreement with a buyer and actually sell the car, an exchange will not take place. Notice that marketing can occur even if an exchange does not occur. In the example just discussed, you would have engaged in marketing even if no one bought your used automobile.

REVIEW LEARNING OUTCOME

LO 1 Define the term *marketing*



LO 2

Marketing Management Philosophies

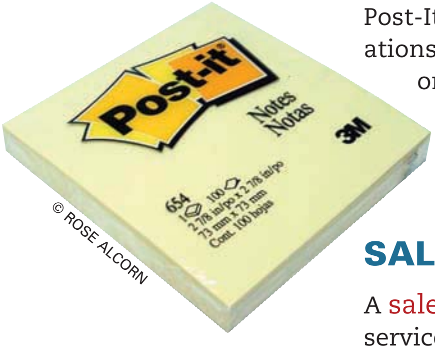
Four competing philosophies strongly influence an organization's marketing processes. These philosophies are commonly referred to as production, sales, market, and societal marketing orientations.

PRODUCTION ORIENTATION

production orientation
A philosophy that focuses on the internal capabilities of the firm rather than on the desires and needs of the marketplace.

A production orientation is a philosophy that focuses on the internal capabilities of the firm rather than on the desires and needs of the marketplace. A production orientation means that management assesses its resources and asks these questions: "What can we do best?" "What can our engineers design?" "What is easy to produce, given our equipment?" In the case of a service organization, managers ask, "What services are most convenient for the firm to offer?" and "Where do our talents lie?" Some have referred to this orientation as a *Field of Dreams* orientation, from the movie's well-known line, "If we build it, they will come." The furniture industry is infamous for its disregard of customers and for its slow cycle times. This has always been a production-oriented industry.

There is nothing wrong with assessing a firm's capabilities; in fact, such assessments are major considerations in strategic marketing planning (see Chapter 2). A production orientation falls short because it does not consider whether the goods and services that the firm produces most efficiently also meet the needs of the marketplace. Sometimes what a firm can best produce is exactly what the market wants. For example, the research and development department of 3M's commercial tape division developed and patented the adhesive component of



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Post-It Notes a year before a commercial application was identified. In other situations, as when competition is weak or demand exceeds supply, a production-oriented firm can survive and even prosper. More often, however, firms that succeed in competitive markets have a clear understanding that they must first determine what customers want and then produce it, rather than focusing on what company management thinks should be produced.

SALES ORIENTATION

A sales orientation is based on the ideas that people will buy more goods and services if aggressive sales techniques are used and that high sales result in high profits. Not only are sales to the final buyer emphasized but intermediaries are also encouraged to push manufacturers' products more aggressively. To sales-oriented firms, marketing means selling things and collecting money.

The fundamental problem with a sales orientation, as with a production orientation, is a lack of understanding of the needs and wants of the marketplace. Sales-oriented companies often find that, despite the quality of their sales force, they cannot convince people to buy goods or services that are neither wanted nor needed.

Some sales-oriented firms simply fail to understand what is important to their customers. Many so-called dot-com businesses that came into existence in the late 1990s are no longer around because they focused on the technology rather than the customer.

Kimberly Knickle couldn't have been happier when she signed up with online grocer Streamline.com. Streamline installed a refrigerator in her garage to make deliveries when she wasn't home, picked up the dry cleaning, delivered stamps, and dropped off parcel shipments. The best part was the customer service. When something went wrong, Streamline instantly credited her account. She could always get someone on the phone. As the company expanded its customer base, however, the deliveries became inconsistent, telephone customer service put her on hold more often, and the company overcharged her several times. The big blow came when it revamped its Web site: in the past, she could place an order for 30 items quickly, but the company switched to a new system that checked inventory in real time, slowing down the interface tremendously. "The grocery store is two minutes away," Knickle says. "In 25 minutes, I could get two-thirds of my shopping done at the store. This was supposed to make my life easier."[6]

sales orientation
The idea that people will buy more goods and services if aggressive sales techniques are used and that high sales result in high profits

marketing concept
The idea that the social and economic justification for an organization's existence is the satisfaction of customer wants and needs while meeting organizational objectives.

market orientation
A philosophy that assumes that a sale does not depend on an aggressive sales force but rather on a customer's decision to purchase a product. It is synonymous with the marketing concept.

MARKET ORIENTATION

The marketing concept is a simple and intuitively appealing philosophy that articulates a market orientation. It states that the social and economic justification for an organization's existence is the satisfaction of customer wants and needs while meeting organizational objectives. It is based on an understanding that a sale does not depend on an aggressive sales force, but rather on a customer's decision to purchase a product. What a business thinks it produces is not of primary importance to its success. Instead, what customers think they are buying—the perceived value—defines a business. The marketing concept includes the following:

- Focusing on customer wants and needs so that the organization can distinguish its product(s) from competitors' offerings
- Integrating all the organization's activities, including production, to satisfy these wants
- Achieving long-term goals for the organization by satisfying customer wants and needs legally and responsibly

Firms that adopt and implement the marketing concept are said to be market oriented. Achieving a market orientation involves obtaining information about

© AP PHOTO/CHUCK BURTON

Wachovia Bank is known for its high-quality service and its focus on continuous improvement in customer satisfaction.

customers, competitors, and markets; examining the information from a total business perspective; determining how to deliver superior customer value; and implementing actions to provide value to customers.

For example, consumers consistently cite Wachovia Bank for its high-quality service. So what is Wachovia doing right? Each month, the bank's senior managers hold a 90-minute session to review the results of independent studies that gauge employee-customer interaction and customer satisfaction.[7] Goals include spotting any problems as early as possible and focusing on continuous improvement in customer satisfaction.

Understanding your competitive arena and competitors' strengths and weaknesses is a critical component of a market orientation. This includes assessing what existing or potential competitors might be intending to do tomorrow as well as what they are doing today. Western Union failed to define its competitive arena as telecommunications, concentrating instead on telegraph services, and was eventually outflanked by fax technology. Had Western Union been a market-oriented company, its management might have better understood the changes taking place, seen the competitive threat, and developed strategies to counter the threat.

societal marketing orientation
The idea that an organization exists not only to satisfy customer wants and needs and to meet organizational objectives, but also to preserve or enhance individuals' and society's long-term best interests.

SOCIETAL MARKETING ORIENTATION

The societal marketing orientation extends the marketing concept by acknowledging that some products that customers want may not really be in their best interests or the best interests of society as a whole. This philosophy, states that an organization exists not only to satisfy customer wants and needs and to meet organizational objectives but also to preserve or enhance individuals' and society's long-term best interests. Marketing products and containers that are less toxic than normal, are more durable, contain reusable materials, or are made of recyclable materials is consistent with a societal marketing orientation. The American Marketing Association's new definition of marketing recognizes the importance of a societal marketing orientation by including "society at large" as one of the constituencies for which marketing seeks to provide value.

Although the societal marketing concept has been discussed for over 30 years, it did not receive widespread support until the early 2000's. Consumers have long said that they favored more environmentally friendly products, but were unwilling to pay a premium price or accept a less effective product. For example, phosphate-free detergents have long been recognized as more environmentally friendly than those containing phosphates. However, consumers have been reluctant to purchase detergents that they perceived were less effective at cleaning clothes. Concerns such as climate change, the depleting ozone layer, fuel shortages, pollution, and raised health concerns have caused

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Although Yoplait is not founded on a societal marketing orientation in the same way as, say, the Sierra Club, the company still communicates to its customers its concern about women's health. For each pink lid redeemed by a Yoplait customer, the company donates 10 cents to the Susan G. Komen Breast Cancer Foundation.

consumers and legislators to be more aware of the need for companies and consumers to adopt measures that conserve resources and cause less damage to the environment.

"This has gone from a niche issue three to five years ago to an extremely important mainstream issue."[8] An NBC Universal audience survey recently revealed that 90 percent of adults ages 19–49 feel it is important to be green, 89 percent think business should be doing more to protect the environment, and 84 percent say they are more likely to use a brand that is environmentally responsible.[9] Another study found that Americans want clean, alternative energy, and they want the government to change U.S. energy policy immediately to make it more available. Seventy-four percent of survey respondents said the country should move to alternative fuels, and 71 percent said that we should expand the use of clean alternative energy.[10]

Companies of all sizes have begun announcing new "green" initiatives.[11] Sears Holdings Corp. has unveiled a new line of high-efficiency appliances, including the Kenmore Elite Ultra Wash dishwasher that uses about half the water of a standard dishwasher. General Electric Co. has introduced several new energy-efficient refrigerators that use at least 15 percent less energy.[12] Coca-Cola Co. plans to build a plant that will be able to recycle two billion 20-ounce bottles a year. The company already has recycling plants in Australia, Austria, Mexico, the Philippines, and Switzerland.[13] Even giant retailer Wal-Mart has new initiatives to become known for environmental sustainability. CEO Lee Scott has announced that new stores will use 30 percent less energy, and existing stores will reduce greenhouse gases by 20 percent. The company hopes to double the gas mileage of its trucking fleet by 2015.[14]

It appears that consumers, manufacturers, and retailers are taking actions that support the societal marketing orientation. Consumers are demonstrating that

GLOBAL Perspectives

McDonald's in Russia

Of the 118 countries where McDonald's Corp. does business, none can boast more activity than Russia. On average, each location serves about 850,000 diners annually—more than twice the average individual store traffic in most other markets McDonald's serves.

This has presented the world's largest restaurant chain with an unusual dilemma. Russia, with its burgeoning middle class and consumer appetites for all things American, is a jewel in the McDonald's system. But the company is being prudent about expansion here—due partly to Russia's famous bureaucracy and partly to the chain's own philosophical shift.

Aggressive growth plans at McDonald's have backfired badly in the past. During the 1990s, the company was fixated on adding restaurants throughout the chain—as many as 2,500 stores a year. But by 2000, the condition of its existing locations, as well as the appeal of certain menu items, deteriorated. Two years later, the company's flawed expansion strategy was hammering its profits and stock price.

Aiming then to be "better, not just bigger," the Oak Brook, Ill., company reined in expansion. In 2003, when McDonald's reported its first-ever quarterly loss, it opened a net of 21 new stores—down from 1,015 in the previous year.

New emphasis was placed on improving signature products such as the Big Mac and Chicken McNuggets. Executives also called for an aesthetic overhaul, using more muted colors and lighting schemes in the stores. The changes helped lift sales and profits, ushering in one of the company's most successful performance streaks to date. McDonald's share rose by 33 percent in the year following these changes.

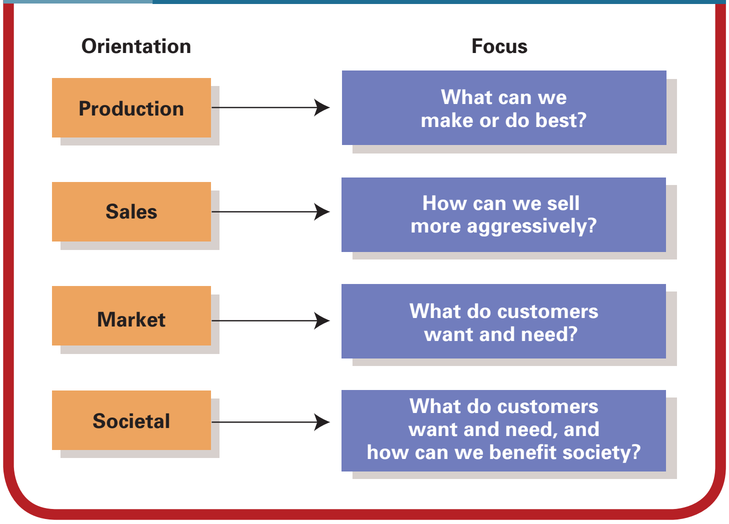
In Russia, the company is now working to squeeze more sales and profits from its 180 existing locations rather than over-rely on new restaurants. To do so, Khamzat Khasbulatov, chief executive of McDonald's Russia, is taking a page from Western-style dining habits. He has introduced a breakfast menu and plans to add more "McCafé" sections serving espresso drinks to draw late afternoon and evening crowds. He is also trying to increase the number of restaurants that have drive-throughs and twenty-four hour service. "You have to keep your restaurants relevant to your consumer," he says. Mr. Khasbulatov is also focusing on ways to move lines and customer traffic more quickly. In some locations, employees take orders on handheld devices before customers reach the counter. Special cooking equipment also hastens the diner's experience. A new toaster, for instance, browns sandwich buns in 14 seconds, less than half what it used to take, according to Karina Pogosova, junior vice president of operations for McDonald's Russia.

Mr. Khasbulatov doesn't want the lines to disappear entirely. "When I said I have too many customers, it's a nice problem to have," he says. "I would love to continue to have this problem."[16]

What marketing management philosophy does McDonald's in Russia appear to be following? Explain.

REVIEW LEARNING OUTCOME

LO 2 Describe four marketing management philosophies



they like to buy from firms that make them feel good.[15] Adopting a societal marketing orientation and clearly communicating this decision and the actions that support it helps firms differentiate themselves from competitors and strengthens their positioning.

This chapter's "Global Perspectives" box illustrates decisions companies face as they try to balance growth and customer satisfaction. Aiming to be "better, not just bigger" is often a difficult challenge for executives who are evaluated primarily on quarterly and annual profit generation.

LO 3 Differences between Sales and Market Orientations

The differences between sales and market orientations are substantial.

The two orientations can be compared in terms of five characteristics: the organization's focus, the firm's business, those to whom the product is directed, the firm's primary goal, and the tools used to achieve those goals.

THE ORGANIZATION'S FOCUS

Personnel in sales-oriented firms tend to be "inward looking," focusing on selling what the organization makes rather than making what the market wants. Many of the historic sources of competitive advantage—technology, innovation, economies of scale—allowed companies to focus their efforts internally and prosper. Today, many successful firms derive their competitive advantage from an external, market-oriented focus. A market orientation has helped companies such as Dell, Inc., the Royal Bank of Canada, and Southwest Airlines outperform their competitors. These companies put customers at the center of their business in ways most companies do poorly or not at all.

A sales orientation has led to the demise of many firms including Streamline.com, the Digital Entertainment Network, and Urban Box Office. As one technology industry analyst put it, "no one has ever gone to a Web site because they heard there was great Java running."[17]

Customer Value

customer value
The relationship between benefits and the sacrifice necessary to obtain those benefits.

Customer value is the relationship between benefits and the sacrifice necessary to obtain those benefits. Customer value is not simply a matter of high quality. A high-quality product that is available only at a high price will not be perceived as a good value, nor will bare-bones service or low-quality goods selling for a low price. Instead, customers value goods and services that are of the quality they expect and that are sold at prices they are willing to pay. Value can be used to sell a Mercedes-Benz as well as a Tyson frozen chicken dinner.

The automobile industry illustrates the importance of creating customer value. To penetrate the fiercely competitive luxury automobile market, Lexus adopted a customer-driven approach, with particular emphasis on service. Lexus stresses product quality with a standard of zero defects in manufacturing. The service quality goal is to treat each customer as one would treat a guest in one's home, to pursue the perfect person-to-person relationship, and to strive to improve continually.

This pursuit has enabled Lexus to establish a clear quality image and capture a significant share of the luxury car market.

Marketers interested in customer value

- *Offer products that perform*: This is the bare minimum requirement. Grocery chains such as Safeway are realizing that the best way to compete against Wal-Mart is not on the basis of price but on the basis of convenience, lesser-known upscale brands, and freshness.[18] In other words, offering customer value in areas where Wal-Mart is relatively weaker.
- *Earn trust*: A stable base of loyal customers enhances a firm's ability to grow and prosper. About 80 percent of Starbucks' revenues come from customers who visit the store an average of 18 times per month.[19]
- *Avoid unrealistic pricing*: E-marketers are leveraging Internet technology to redefine how prices are set and negotiated. With lower costs, e-marketers can often offer lower prices than their brick-and-mortar counterparts. The enormous popularity of auction sites such as eBay and Amazon.com and the customer-bid model used by Priceline illustrates that online customers are interested in bargain prices. Many are not willing to pay a premium for the convenience of examining the merchandise and taking it home with them. Others will gladly pay a premium for an experience that is not only functionally, but emotionally rewarding. Executives at Starwood Hotels and Resorts' "W" chain believe that they are able to make an emotional connection when customers walk through the door of their hotel room and see the bed with clean-looking, sumptuous linens and other amenities.[20]
- *Give the buyer facts*: Today's sophisticated consumer wants informative advertising and knowledgeable salespeople. Web sites that don't provide enough information are among the top ten things that "irk" Internet shoppers most.
- *Offer organization-wide commitment in service and after-sales support*: People fly Southwest Airlines because the airline offers superior value. Although passengers do not get assigned seats or meals (just peanuts or crackers) when they use the airline, its service is reliable and friendly and costs less than most major airlines. All Southwest employees are involved in the effort to satisfy customers. Pilots tend to the boarding gate when their help is needed, and ticket agents help move luggage. One reservation agent flew from Dallas to Tulsa with a frail, elderly woman whose son was afraid she couldn't handle the change of planes by herself on her way to St. Louis.
- *Co-Creation*: Some companies and products allow customers to help create their own experience. For example, TiVo allows people to watch chosen TV shows when they want to watch them. As one loyal customer exclaimed, "TiVo has changed my life!"[21]

customer satisfaction
Customers' evaluation of a good or service in terms of whether it has met their needs and expectations.

© COURTESY OF SOUTHWEST AIRLINES

Southwest Airlines was recently named one of *BusinessWeek's* "Customer Service Champs," and has ranked in as one of "America's Top Ten" most admired corporations by *Fortune* magazine for 11 consecutive years.

Customer Satisfaction

Customer satisfaction is the customer's evaluation of a good or service in terms of whether that good or service has met the customer's needs and expectations. Failure to meet needs and expectations results in dissatisfaction with the good or service.[22] Some companies, in their passion to drive down costs, have damaged their relationships with customers. Dell Computers, Home Depot, and Northwest Airlines are examples of companies where executives lost track of the delicate balance between efficiency and service.[23] Each has realized change is needed and have implemented improvements. Firms that have a reputation for delivering high levels of customer satisfaction do things differently from their competitors. Top management is obsessed with customer satisfaction, and employees throughout the organization understand the link between their job and satisfied customers. The culture of the organization is to focus on delighting customers rather than on selling products.

Nordstrom's impeccable reputation for customer service comes not from its executives or its marketing team, but from the customers themselves. The retail giant is willing to take risks, do unusual and often expensive favors for shoppers, and reportedly even accept returns on items not purchased there. Still, they keep improving. The company recently installed a new database enabling salespeople to assist customers in locating items in inventory somewhere in the chain, but not in a particular store. Customers can then purchase these items online.[24]

Building Relationships

Attracting new customers to a business is only the beginning. The best companies view new-customer attraction as the launching point for developing and enhancing a long-term relationship. Companies can expand market share in three ways: attracting new customers, increasing business with existing customers, and retaining current customers. Building relationships with existing customers directly addresses two of the three possibilities and indirectly addresses the other.

relationship marketing
A strategy that focuses on keeping and improving relationships with current customers.

Relationship marketing is a strategy that focuses on keeping and improving relationships with current customers. It assumes that many consumers and business customers prefer to have an ongoing relationship with one organization than to switch continually among providers in their search for value.[25] USAA is a good example of a company focused on building long-term relationships with customers. In 2007, a *Business Week*/J.D. Powers & Associates survey ranked USAA as the top provider of customer service among U.S. firms.[26] Customer retention was a core value of the company long before customer loyalty became a popular business concept. USAA believes so strongly in the importance of customer retention that managers and executives' bonuses are based, in part, on this dimension.[27]

Most successful relationship marketing strategies depend on customer-oriented personnel, effective training programs, employees with authority to make decisions and solve problems, and teamwork.

Customer-Oriented Personnel

For an organization to be focused on building relationships with customers, employees' attitudes and actions must be customer oriented. An employee may be the only contact a particular customer has with the firm. In that customer's eyes, the employee is the firm. Any person, department, or division that is not customer-oriented weakens the positive image of the entire organization. For example, a potential customer who is greeted discourteously may well assume that the employee's attitude represents the whole firm.

Some companies, such as Coca-Cola, Delta Air Lines, Hershey Company, Kellogg, Nautilus, and Sears, have appointed chief customer officers (CCOs). These customer advocates provide an executive voice for customers and report directly to the CEO. Their responsibilities include assuring that the company maintains a customer-centric culture and that all company employees remain focused on delivering customer value.

The Role of Training

Leading marketers recognize the role of employee training in customer service and relationship building. Sue Noles, senior vice president of sales and customer service at T-Mobile, believes that making the customer happy is a lot easier to do when employees actually like their jobs and feel that what they do matters.[28] Sales staff at The Container Store receive over 240 hours of training and generous benefits compared to an industry average of eight hours training and modest benefits. According to Kip Kindell, CEO and Co-Chairman of The Container

Store, "if you take care of your employees, they'll take care of the customer—and that will take care of your shareholders."[29]

empowerment
Delegation of authority to solve customers' problems quickly—usually by the first person that the customer notifies regarding a problem.

teamwork
Collaborative efforts of people to accomplish common objectives.

Empowerment In addition to training, many market-oriented firms are giving employees more authority to solve customer problems on the spot. The term used to describe this delegation of authority is **empowerment.** Employees develop ownership attitudes when they are treated like part-owners of the business and are expected to act the part. These employees manage themselves, are more likely to work hard, account for their own performance and the company's, and take prudent risks to build a stronger business and sustain the company's success. FedEx customer service representatives are trained and empowered to resolve customer problems. Although the average FedEx transaction costs only $16, the customer service representatives are empowered to spend up to $100 to resolve a customer problem.

At Wegmans Food Markets, employees are encouraged to do just about anything on the spot, without consulting a higher-up, to satisfy a customer. That could entail cooking a family's Thanksgiving turkey at the store because the one purchased was too big to fit in the family's oven or going to a customer's home to rescue a meal. Empowering employees goes beyond having them make house calls, though. It means creating an environment where employees can do the right things, unburdened by hierarchies. According to Heather Pawlowski, a Wegmans vice president, "We're taking customers to a place they've not been before. And once they arrive, shoppers don't want to leave."[30]

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Empowerment gives customers the feeling that their concerns are being addressed and gives employees the feeling that their expertise matters. The result is greater satisfaction for both customers and employees.

Teamwork Many organizations that are frequently noted for delivering superior customer value and providing high levels of customer satisfaction, such as Southwest Airlines and Walt Disney World, assign employees to teams and teach them team-building skills. **Teamwork** entails collaborative efforts of people to accomplish common objectives. Job performance, company performance, product value, and customer satisfaction all improve when people in the same department or work group begin supporting and assisting each other and emphasize cooperation instead of competition. Performance is also enhanced when cross-functional teams align their jobs with customer needs. For example, if a team of telecommunications service representatives is working to improve interaction with customers, back-office people such as computer technicians or training personnel can become part of the team with the ultimate goal of delivering superior customer value and satisfaction.

THE FIRM'S BUSINESS

A sales-oriented firm defines its business (or mission) in terms of goods and services. A market-oriented firm defines its business in terms of the benefits its customers seek. People who spend their money, time, and energy expect to receive benefits, not just goods and services. This distinction has enormous implications.

Because of the limited way it defines its business, a sales-oriented firm often misses opportunities to serve customers whose wants can be met through a wide range of product offerings instead of specific products. For example, in 1989, 220-year-old Britannica had estimated revenues of $650 million and a worldwide sales force of 7,500. Just five years later, after three consecutive years of losses, the sales force had collapsed to as few as 280 representatives. How did this respected company sink so low? Britannica managers saw that competitors were beginning to use CD-ROMs to store huge masses of information, but chose to ignore the new

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computer technology, as well as an offer to team up with Microsoft.

It's not hard to see why parents would rather give their children an encyclopedia on a compact disc instead of a printed one. The CD-ROM versions were either given away or sold by other publishers for under $400. A full 32-volume set of *Encyclopaedia Britannica* weighs about 120 pounds, costs a minimum of $1,500, and takes up four and one-half feet of shelf space. If Britannica had defined its business as providing information instead of publishing books, it might not have suffered such a precipitous fall.

Adopting a "better late than never" philosophy, Britannica has made its complete 32-volume set available free on the Internet. The company no longer sells door-to-door and hopes to return to profitability by selling advertising on its Web site.

Answering the question "What is this firm's business?" in terms of the benefits customers seek, instead of goods and services, offers at least three important advantages:

- It ensures that the firm keeps focusing on customers and avoids becoming preoccupied with goods, services, or the organization's internal needs.
- It encourages innovation and creativity by reminding people that there are many ways to satisfy customer wants.
- It stimulates an awareness of changes in customer desires and preferences so that product offerings are more likely to remain relevant.

Having a market orientation and focusing on customer wants do not mean that customers will always receive everything they want. It is not possible, for example, to profitably manufacture and market automobile tires that will last for 100,000 miles for $25. Furthermore, customers' preferences must be mediated by sound professional judgment as to how to deliver the benefits they seek. As one adage suggests, "People don't know what they want—they only want what they know." Consumers have a limited set of experiences. They are unlikely to request anything beyond those experiences because they are not aware of benefits they may gain from other potential offerings. For example, before the Internet, many people thought that shopping for some products was boring and time consuming, but could not express their need for electronic shopping.

THOSE TO WHOM THE PRODUCT IS DIRECTED

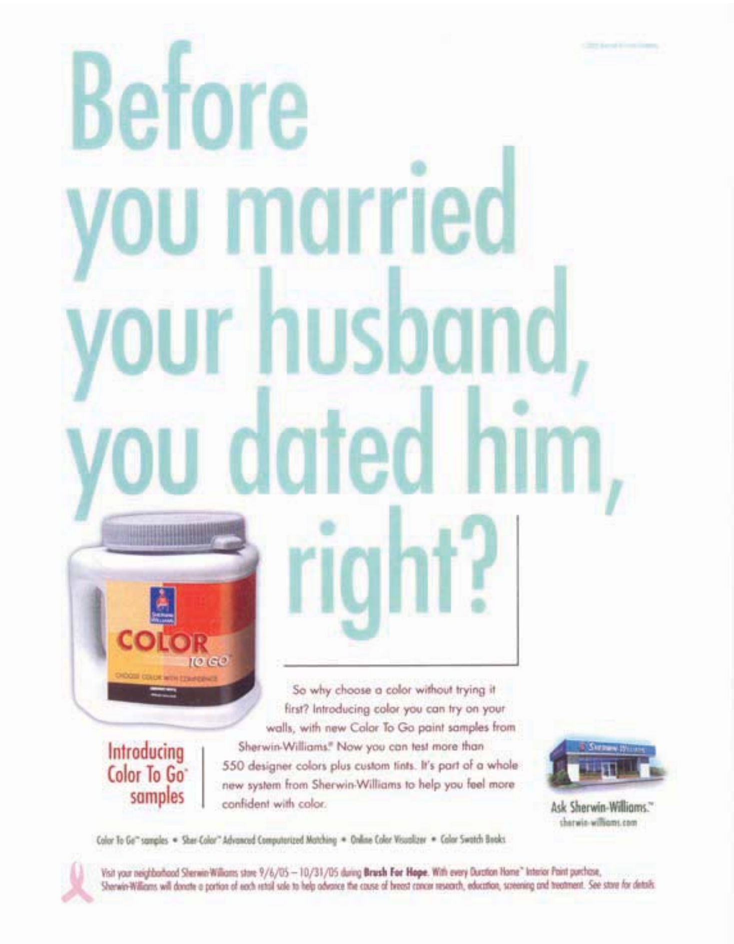
A sales-oriented organization targets its products at "everybody" or "the average customer." A market-oriented organization aims at specific groups of people. The fallacy of developing products directed at the average user is that relatively few average users actually exist. Typically, populations are characterized by diversity. An average is simply a midpoint in some set of characteristics. Because most potential customers are not "average," they are not likely to be attracted to an average product marketed to the average customer. Consider the market for shampoo as one simple example. There are shampoos for oily hair, dry hair, and dandruff. Some shampoos remove the gray or color hair. Special shampoos are marketed for infants and elderly people. There is even shampoo for people with average or normal hair (whatever that is), but this is a fairly small portion of the total market for shampoo.

A market-oriented organization recognizes that different customer groups want different features or benefits. It may therefore need to develop different goods, services, and promotional appeals. A market-oriented organization carefully analyzes the market and divides it into groups of people who are fairly similar in terms of selected characteristics. Then the organization develops marketing programs that will bring about mutually satisfying exchanges with one or more of those groups.

Paying attention to the customer isn't exactly a new concept. Back in the 1920s, General Motors began designing cars for every lifestyle and pocketbook. This was a breakthrough for an industry that had been largely driven by production needs ever since Henry Ford promised any color as long as it was black. Chapter 8 thoroughly explores the topic of analyzing markets and selecting those that appear to be most promising to the firm.

THE FIRM'S PRIMARY GOAL

A sales-oriented organization seeks to achieve profitability through sales volume and tries to convince potential customers to buy, even if the seller knows that the customer and product are mismatched. Sales-oriented organizations place a higher premium on making a sale than on developing a long-term relationship with a customer. In contrast, the ultimate goal of most market-oriented organizations is to make a profit by creating customer value, providing customer satisfaction, and building long-term relationships with customers. The exception is so-called nonprofit organizations that exist to achieve goals other than profits. Nonprofit organizations can and should adopt a market orientation. Nonprofit organization marketing is explored further in Chapter 12.



A market-oriented organization uses many tools to promote its products. Sherwin-Williams uses a variety of promotional activities, including advertising and offering free samples, to market its paints.

TOOLS THE ORGANIZATION USES TO ACHIEVE ITS GOALS

Sales-oriented organizations seek to generate sales volume through intensive promotional activities, mainly personal selling and advertising. In contrast, market-oriented organizations recognize that promotion decisions are only one of four basic marketing mix decisions that have to be made: product decisions, place (or distribution) decisions, promotion decisions, and pricing decisions. A market-oriented organization recognizes that each of these four components is important. Furthermore, market-oriented organizations recognize that marketing is not just a responsibility of the marketing department. Interfunctional coordination means that skills and resources throughout the organization are needed to create, communicate, and deliver superior customer service and value.

A WORD OF CAUTION

This comparison of sales and market orientations is not meant to belittle the role of promotion, especially personal selling, in the marketing mix. Promotion is the means by which organizations communicate with present and prospective customers about the merits and characteristics of their organization and products. Effective promotion is an essential part of effective marketing. Salespeople who work for market-oriented organizations are generally perceived by their customers to be problem solvers and important links to supply sources and new products. Chapter 18 examines the nature of personal selling in more detail.

REVIEW LEARNING OUTCOME

LO3 Discuss the differences between sales and market orientations

	What is the organization's focus?	What business are you in?	To whom is the product directed?	What is your primary goal?	How do you seek to achieve your goal?
Sales Orientation	Inward, on the organization's needs	Selling goods and services	Everybody	Profit through maximum sales volume	Primarily through intensive promotion
Market Orientation	Outward, on the wants and preferences of customers	Satisfying customer wants and needs and delivering superior value	Specific groups of people	Profit through customer satisfaction	Through coordinated marketing and interfunctional activities

LO4

Why Study Marketing?

Now that you understand the meaning of the term *marketing*, why it is important to adopt a marketing orientation, how organizations implement this philosophy, and how one-to-one marketing is evolving, you may be asking, "What's in it for me?" or "Why should I study marketing?" These are important questions, whether you are majoring in a business field other than marketing (such as accounting, finance, or management information systems) or a nonbusiness field (such as journalism, economics, or agriculture). There are several important reasons to study marketing: Marketing plays an important role in society, marketing is important to businesses, marketing offers outstanding career opportunities, and marketing affects your life every day.

MARKETING PLAYS AN IMPORTANT ROLE IN SOCIETY

The total population of the United States exceeds 300 million people.[31] Think about how many transactions are needed each day to feed, clothe, and shelter a population of this size. The number is huge. And yet it all works quite well, partly because the well-developed U.S. economic system efficiently distributes the output of farms and factories. A typical U.S. family, for example, consumes 2.5 tons of food a year. Marketing makes food available when we want it, in desired quantities, at accessible locations, and in sanitary and convenient packages and forms (such as instant and frozen foods).

MARKETING IS IMPORTANT TO BUSINESS

The fundamental objectives of most businesses are survival, profits, and growth. Marketing contributes directly to achieving these objectives. Marketing includes the following activities, which are vital to business organizations: assessing the wants and satisfactions of present and potential customers, designing and managing product offerings, determining prices and pricing policies, developing distribution strategies, and communicating with present and potential customers.

All businesspeople, regardless of specialization or area of responsibility, need to be familiar with the terminology and fundamentals of accounting, finance, management, and marketing. People in all business areas need to be able to communicate with specialists in other areas. Furthermore, marketing is not just a job done by people in a marketing department. Marketing is a part of the job of everyone in the organization. Therefore, a basic understanding of marketing is important to all businesspeople.

MARKETING OFFERS OUTSTANDING CAREER OPPORTUNITIES

Between a fourth and a third of the entire civilian workforce in the United States performs marketing activities. Marketing offers great career opportunities in such areas as professional selling, marketing research, advertising, retail buying, distribution management, product management, product development, and wholesaling. Marketing career opportunities also exist in a variety of nonbusiness organizations, including hospitals, museums, universities, the armed forces, and various government and social service agencies. (See Chapter 12.)

As the global marketplace becomes more challenging, companies all over the world and of all sizes are going to have to become better marketers. For a comprehensive look at career opportunities in marketing and a variety of other useful information about careers, read the Career Appendix at the end of this chapter and visit our Web site at http://www.cengage.com/marketing/lamb.

REVIEW LEARNING OUTCOME

LO4 Describe several reasons for studying marketing

MARKETING AFFECTS YOUR LIFE EVERY DAY

Marketing plays a major role in your everyday life. You participate in the marketing process as a consumer of goods and services. About half of every dollar you spend pays for marketing costs, such as marketing research, product development, packaging, transportation, storage, advertising, and sales expenses. By developing a better understanding of marketing, you will become a better-informed consumer. You will better understand the buying process and be able to negotiate more effectively with sellers. Moreover, you will be better prepared to demand satisfaction when the goods and services you buy do not meet the standards promised by the manufacturer or the marketer.

Number of competing marketing philosophies (or orientations) that influence an organization's marketing processes > **4**

240 < Number of training hours/year for The Container Store sales staff

Number of sales staff training hours/year retail industry average > **8**

16 < The dollar cost of the average FedEx transaction

The dollar amount FedEx customer service reps are empowered to spend to resolve a customer problem > **100**

2.5 < Tons of food a typical U.S. family consumes each year

Review and Applications

LO 1

Define the term *marketing*. Marketing is the activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large.

ONLINE

1.1 What is the AMA? What does it do? How do its services benefit marketers?
http:// www.marketingpower.com

LO 2

Describe four marketing management philosophies. The role of marketing and the character of marketing activities within an organization are strongly influenced by its philosophy and orientation. A production-oriented organization focuses on the internal capabilities of the firm rather than on the desires and needs of the marketplace. A sales orientation is based on the beliefs that people will buy more products if aggressive sales techniques are used and that high sales volumes produce high profits. A market-oriented organization focuses on satisfying customer wants and needs while meeting organizational objectives. A societal marketing orientation goes beyond a market orientation to include the preservation or enhancement of individuals' and society's long-term best interests.

WRITING

2.1 Your company president has decided to restructure the firm to make it more market oriented. She is going to announce the changes at an upcoming meeting. She has asked you to prepare a short speech outlining the general reasons for the new company orientation.

2.2 Donald E. Petersen, former chairman of the board of Ford Motor Company, remarked, "If we aren't customer driven, our cars won't be either." Explain how this statement reflects the marketing concept.

2.3 Give an example of a company that might be successfully following a production orientation. Why might a firm in this industry be successful following such an orientation?

LO 3

Discuss the differences between sales and market orientations. First, sales-oriented firms focus on their own needs; market-oriented firms focus on customers' needs and preferences. Second, sales-oriented companies consider themselves to be deliverers of goods and services, whereas market-oriented companies view themselves as satisfiers of customers. Third, sales-oriented firms direct their products to everyone; market-oriented firms aim at specific segments of the population. Fourth, although the primary goal of both types of firms is profit, sales-oriented businesses pursue maximum sales volume through intensive promotion, whereas market-oriented businesses pursue customer satisfaction through coordinated activities.

3.1 A friend of yours agrees with the adage "People don't know what they want—they only want what they know." Write your friend a letter expressing the extent to which you think marketers shape consumer wants.

WRITING

3.2 Your local supermarket's slogan is "It's your store." However, when you asked one of the stock people to help you find a bag of chips, he told you it was not his job and that you should look a littler harder. On your way out, you noticed a sign with an address for complaints. Draft a letter explaining why the supermarket's slogan will never be credible unless the employees carry it out.

ONLINE

3.3 How does Philip Morris handle the sensitive issues associated with marketing tobacco? What kind of information does its Web site at http://www.philipmorris.com/ provide about smoking and its negative effects on health? How do you think Philip Morris is able to justify such marketing tactics? After checking around the site, do you think that approach makes the company more or less trustworthy?

LO 4

Describe several reasons for studying marketing. First, marketing affects the allocation of goods and services that influence a nation's economy and standard of living. Second, an understanding of marketing is crucial to understanding most businesses. Third, career opportunities in marketing are diverse, profitable, and expected to increase significantly during the coming decade. Fourth, understanding marketing makes consumers more informed.

WRITING

4.1 Write a letter to a friend or family member explaining why you think that a course in marketing will help you in your career in some field other than marketing.

Key Terms

customer satisfaction	9	market orientation	5	relationship marketing	10
customer value	8	marketing	3	sales orientation	5
empowerment	11	marketing concept	5	societal marketing orientation	6
exchange	3	production orientation	4	teamwork	11

Exercises

APPLICATION EXERCISE

Understanding the differences among the various marketing management philosophies is the starting point for understanding the fundamentals of marketing.[32] From reading the chapter, you may be convinced that the market orientation is the most appealing philosophy and the one best suited to creating a competitive advantage. Not all companies, however, use the market orientation. And even companies that follow it may not execute well in all areas.

Activities

1. Visit your local grocery store and go through the cereal, snack-food, and dental hygiene aisles. Go up and down each aisle slowly, noticing how many different products are available and how they are organized on the shelves.
2. Count the varieties of product in each product category. For example, how many different kinds of cereal are on the shelves? How many different sizes? Do the same for snack food and toothpaste.
3. Now try to find a type of product in the grocery store that does not exhibit such variety. There may not be many. Why do you think there are enough kinds of cereals to fill an entire aisle (and then some), but only a few different types of, say, peanut butter? Can this difference be explained in terms of marketing management philosophy (peanut butter manufacturers do not follow the marketing concept) or by something else entirely?
4. Have you ever wanted to see a particular kind of cereal or snack food on the shelf? Think of product varietals (like grapefruit-flavored toothpaste or peanut butter-covered popcorn) that you have never seen on the shelf but would be interested in trying if someone would make it. Write a letter or send an e-mail to an appropriate company, suggesting that it add your concept to its current product line.

ETHICS

ETHICS EXERCISE

In today's business environment, ethics are extremely important. In recent years, there have been numerous scandals and trials that stem from a lack of ethical judgment. For this reason, we are including an ethical exercise in every chapter. A brief scenario will present you with a situation in which the right thing to do may or may not be crystal clear, and you will need to decide the ethical way out of the dilemma.

Rani Pharmaceuticals is the maker of several popular drugs used to treat high blood pressure and arthritis. Over time, the company has developed a positive relationship with many of the patients who use its medications through a quarterly newsletter that offers all the latest information on new medical research findings and general health and fitness articles. The company has just been acquired by a group of investors who also own Soothing Waters Hot Tubs and Spas. The marketing director for Soothing Waters would like to use Rani's mailing list for a direct-mail promotion.

Questions

1. What should Rani Pharmaceuticals do?
2. Do you think it is ethical to use customer information across multiple divisions of the same company? Explain.
3. To which marketing management philosophy do you think the marketing director for Soothing Waters subscribes? Explain.

Case Study: Netflix

© AP PHOTO/PAUL SAKUMA

READY FOR PRIMETIME

Shocked at the $40 fee he incurred for a late return of *Apollo* 13, Netflix founder Reed Hastings decided that in the age of the Internet, there had to be a better way to rent videos for home viewing. Thus, in 1997, he started an Internet-based, DVD rental service that offered direct-to-home deliveries with no late fees. A mere decade and 8 million subscribers later, Netflix has taken on established video rental companies such as Blockbuster, Hollywood Video, and Wal-Mart and emerged as the leader in innovation and customer service.

In addition to betting that the Internet would be the future of the video rental market, Hastings made a few other key predictions that helped him develop a company with almost $700 million in revenue in under ten years. He watched as moviegoers fled public theaters for the comfort of home theater systems, and he observed those same consumers embracing the features, capacity, and high-quality format of the DVD. Realizing that the Internet could allow those same convenience seekers 24-hour browsing and selection access to an unprecedented volume of movie titles in a single digital catalog, Hastings shrewdly designed a service that outperforms traditional, store-based video rentals.

Netflix allows consumers to choose from a variety of subscription plans. The most popular plan offers three DVDs for $16.99 per month. Once a subscriber builds a list of favorite movies and TV shows from a selection of over 100,000 titles, Netflix mails out the three titles at the top of the list, along with return-addressed prestamped envelopes. After viewing the DVDs, the customer simply mails them back to Netflix in the supplied packaging. When the titles are scanned in at one of the distribution warehouses, the customer is simultaneously sent the next selections on the favorites list.

With over 100 strategically placed distribution centers, Netflix can deliver 95 percent of its movies within one day of being ordered. That outstanding delivery service is just the tip of the iceberg. Netflix's Web site takes personalization to new levels through its high-powered recommendation software, called Cinematch. Cinematch uses over a million lines of code and over half a billion customer-supplied ratings to suggest rental choices upon request.

Amazingly, over 60 percent of the titles added to users' favorites lists comes from Cinematch recommendations, and over a million ratings are sent to Netflix every day. Just how effective is Cinematch? Netflix uses fewer than 50 customer service reps to support its entire customer base! Of those, 10 are authorized to make direct callbacks to customers with complaints to find out how the problem could have been prevented in the first place. It's that kind of attention to customers that forced retail giant Wal-Mart to give up and turn over its entire customer list to Netflix.

Netflix even added two key features to its service in response to customer requests. The first is the ability to generate multiple favorites lists for a single account, allowing families to build multiple wish lists that can differ as much as *Steel Magnolias* and *Old School*. The second is the addition of a community feature called "Friends." Friends enables users to share the titles, ratings, and preferences for recently viewed shows with those they invite to be part of their network.

Always looking to the future, Hastings wants to diversify Netflix by adding high-definition DVD rentals to its current service, selling previously rented DVDs in the rapidly growing used-DVD market, and developing an on-demand video download service. Though it's impossible to tell exactly what blockbuster service Netflix will deliver next, it's a safe bet its customers will applaud.[33]

Questions

1. Describe the elements of the exchange process as they occur between Netflix and its customers.
2. Which marketing management philosophy does Netflix subscribe to?
3. How does Netflix's approach to relationship marketing increase customer satisfaction?

Company Clips

METHOD – LIVE CLEAN

method, the innovative branding concept in household cleaning, was conceived by roommates Eric Ryan and Adam Lowry during their drive to a ski lodge. Eric had been thinking of ways to introduce design to the home care industry (i.e., cleaning products) and began talking about his vision to Adam. A chemical engineer from Stanford University with a degree in environmental science, Adam was the perfect sounding board. He soon realized that he could use his expertise to create naturally-derived, biodegradable formulas for the beautiful products Eric had in mind.

Questions

1. Is method best described as having a market orientation or a societal-marketing orientation?
2. How does method implement the marketing concept?

Marketing & You Results

The higher your score, the more likely you are to do business with the company you thought of and recommend it to others. That is you have a commitment to the organization and are likely a loyal customer. As you read in Chapter 1, building relationships is a central part of the market orientation!

A Career Appendix

One of the most important decisions in your life is choosing a career. Not only will your career choice affect your income and lifestyle, but it also will have a major impact on your happiness and self-fulfillment.

You can use many of the basic concepts of marketing introduced in this book to get the career you want by marketing yourself. The purpose of marketing is to create exchanges that satisfy individual as well as organizational objectives, and a career is certainly an exchange situation for both you and an organization. The purpose of this appendix is to help you market yourself to prospective employers by providing some helpful tools and information.

AVAILABLE CAREERS

Marketing careers have a bright outlook into the next decade. The U.S. Bureau of Labor Statistics estimates that employment in marketing fields will grow between 21 and 35 percent through 2012. Many of these increases will be in the areas of sales, public relations, retailing, advertising, marketing research, product management, and marketing management.

- ***Sales:*** There are more opportunities in sales than in any other area of marketing. Sales positions vary greatly among companies. Some selling positions focus more on providing information; others emphasize locating potential customers, making presentations to committees, and closing the sale. Because compensation is often in the form of salary plus commission, there are few limits on the amount of money a person can make and therefore great potential. Sales positions can be found in many organizations, including manufacturing, wholesaling, retailing, insurance, real estate, financial services, and many other service businesses.
- ***Public relations:*** Public relations firms help create an image or a message for an individual or organization and communicate it effectively to a desired audience. All types of firms, profit and nonprofit organizations, individuals, and even countries employ public relations specialists. Communication skills, both written and oral, are critical for success in public relations.
- ***Retailing:*** Retail careers require many skills. Retail personnel may manage a sales force or other personnel, select and order merchandise, and be responsible for promotional activities, inventory control, store security, and accounting. Large retail stores have a variety of positions, including store or department manager, buyer, display designer, and catalog manager.
- ***Advertising:*** Many organizations employ advertising specialists. Advertising agencies are the largest employers; however, manufacturers, retailers, banks, radio and television stations, hospitals, and insurance agencies all have advertising departments. Creativity, artistic talent, and communication skills are a few of the attributes needed for a successful career in advertising. Account executives serve as a liaison between the advertising agency and the client. Account executives must have a good knowledge of business practices and possess excellent sales skills.
- ***Marketing management:*** Marketing managers develop the firm's detailed marketing strategy. With the help of subordinates, including market research managers and product development managers, they determine the demand for products and services offered by the firm and its competitors. In addition, they identify potential markets—for example, business firms, wholesalers, retailers, government, or the general public. Marketing managers develop pricing strategy with an eye toward maximizing the firm's share of the market and its profits while ensuring that the firm's customers are satisfied. In collaboration with sales, product development, and other managers, they monitor trends that indicate the need for new products and services and oversee product development. Marketing managers work with advertising and promotion managers to promote the firm's products and services and to attract potential users.

Exhibit 1

The FAB Matrix

Need of Employer This job requires . . .	Feature of Job Applicant I have . . .	Advantage of Feature This feature means that . . .	Benefit to Employer You will . . .
• Frequent sales presentations to individuals and groups.	• Taken 10 classes that required presentations.	• I require limited or no training in making presentations.	• Save on the cost of training and have an employee with the ability and confidence to be productive early.
• Knowledge of personal computers, software, and applications.	• Taken a personal computer course and used Lotus in most upper-level classes.	• I can already use Word, Excel, dBase, SAS, SPSS, and other software.	• Save time and money on training.
• A person with management potential.	• Been president of a student marketing group and social fraternity president for two years.	• I have experience leading people.	• Save time because I am capable of stepping into a leadership position as needed.

- ***Marketing research:*** The most rapid growth in marketing careers is in marketing research. Marketing research firms, advertising agencies, universities, private firms, nonprofit organizations, and governments provide growing opportunities in marketing research. Researchers conduct industry research, advertising research, pricing and packaging research, new-product testing, and test marketing. Researchers are involved in one or more stages of the research process, depending on the size of the organization conducting the research. Marketing research requires knowledge of statistics, data processing and analysis, psychology, and communication.
- ***Product management:*** Product managers coordinate all or most of the activities required to market a product. Thus, they need a general knowledge of all aspects of marketing. Product managers are responsible for the successes and failures of a product and are compensated well for this responsibility. Most product managers have previous sales experience and skills in communication. The position of product manager is a major step in the career path of top-level marketing executives.

Starting in a marketing job is also one of the *best routes to the top* of any organization. More CEOs come from sales and marketing backgrounds than from any other field. As examples, Lee Iacocca (Chrysler), Phil Lippincott (Scott Paper), John Akers (IBM), John Sparks (Whirlpool), and Bruno Bich (Bic Pen) came up through sales and marketing. Typically, a college graduate enters the marketing field in a sales position, then moves to sales supervisor, and next sales manager at the district, regional, and national levels. Individuals who prefer to advance through the ranks of marketing management can usually make a career move into product or brand management or another marketing headquarters job after serving for a couple of years in the initial sales position.

Probably the most difficult part of job hunting is deciding exactly what type of work you would like. Many students have had no working experience other than summer jobs, so they are not sure what career to pursue. Too often, college students and their parents rush toward occupational fields that seem to offer the highest monetary payoff or are currently "hot," instead of looking at the long run over a 40- to 50-year working life. One straightforward approach to deciding what type of job to undertake is to do a "self-analysis." This involves honestly asking yourself what your skills, abilities, and interests really are and then identifying occupational fields that match up well with your personality profile. Some students prefer to take various vocational aptitude tests to help identify their interests and abilities. Your college's placement office or psychology department can inform you about the availability of these tests. You may find it useful to develop a FAB (feature–advantage–benefit) matrix that shows what your skills are, why they offer an advantage, and how they would benefit an employer. Exhibit 1 shows an example.

YOUR FIRST MARKETING ASSIGNMENT

Marketing yourself to a prospective employer will usually be your first big marketing assignment. With your services (as represented by your qualifications, education, training, and personal characteristics) as the product, you must convince prospective employers that they should buy your services over those of many other candidates for the job. All the steps of the marketing and sales process apply: identifying opportunities, developing yourself as a product, prospecting for potential employers, planning your approach to them, approaching with a résumé and cover letter, making your sales presentation and demonstrating your qualifications in a personal interview, dealing with objections or giving reasons why the employer should hire you over other candidates, attempting to close the sale by enthusiastically asking for the job and employing appropriate closing techniques, and following up by thanking the prospective employer for the interview and reinforcing a positive impression.

Prospecting for a Potential Employer

After you have determined what you're selling (your skills, abilities, interests, and so forth) and identified the type of job you think you would like, you might begin your personal selling process by looking at the *College Placement Annual* at your college placement office. The *College Placement Annual* provides a variety of information about prospective employers and lists the organizations according to the types of jobs they have available—for example, advertising, banking, marketing research, and sales. Another very important source is an online search on the Internet. Other sources of information about prospective employers include directories such as those published by Dun and Bradstreet, Standard & Poor's, and trade associations; the annual American Marketing Association membership directory (company listings); the Yellow Pages of telephone books in cities where you would like to live and work; and classified sections of the *Wall Street Journal* or city newspapers. Before contacting a particular company, look up its annual report and stock evaluation (from *Value Line* or various other sources) in your college library to learn as much as possible about the company and its prospects for the future. You might also obtain a list of articles on the company from the *Business Periodicals Index (BPI)*.

College Placement Office

Use your college placement office to find out which companies are going to be interviewing on campus on what dates; then sign up for interviews with those companies that seem to best match your job skills and requirements. Usually, the college placement office has books, pamphlets, or files that will give you leads on other prospective employers that may not be interviewing on campus that term.

Job-Hunting Expenses

Although campus interviews are convenient, students seldom get a job without follow-up interviews with more senior managers—usually at company headquarters. These additional interviews generally take a full day and may involve long-distance trips. You should be forewarned that job hunting can be expensive. Printing your résumé, typing cover letters, buying envelopes and stamps, making long-distance telephone calls, incurring travel expenses, and buying new clothing will require a sizable outlay of money. Even though most companies eventually reimburse you for expenses incurred on a company visit, they seldom pay in advance. Reimbursement can take several weeks, so you may encounter some cash-flow problems over the short run.

Exhibit 2

Helpful Internet Addresses for Job Searches/Résumé Writing

The Monster board	**http://www.monster.com**
JobWeb	**http://www.jobweb.org**
Career Mosaic	**http://www.careermosaic.com**
Proven Resumes.com	**http://www.provenresumes.com**
WSJ Career Journal	**http://www.careerjournal.com**

The Internet

The Internet is the fastest-growing medium for job searching today. Many companies are using the Internet to assist them in their recruiting efforts. Some companies are even conducting initial interviews online via videoconferencing. Just as some companies post jobs on a bulletin board, companies can list job opportunities on job posting Web sites. Some of the more popular job search Web sites are listed in Exhibit 2. These sites also contain information about résumé writing and interviewing, as well as tips that you can use to secure the job that you want.

Employment Agencies

Although many employment agencies receive fees from employers for providing good job candidates, others charge job seekers huge fees (sometimes thousands of dollars) for helping them find jobs. Therefore, make sure you fully understand the fee arrangement before signing up with an employment agency. Some employment agencies may not be worth your time and/or money because they use a programmed approach to helping you write your résumé and cover letter and prospect for potential employers. Potential employers have seen these "canned" formats and approaches so many times that your personal advertisement (your résumé and cover letter) will be almost indistinguishable from others.

The Hidden Job Market

It has been estimated that nearly 90 percent of available jobs are never advertised and never reach employment agency files, so creative resourcefulness often pays off in finding the best jobs. Consider every reasonable source for leads. Sometimes your professors, deans, or college administrators can give you names and contact persons at companies that have hired recent graduates.

Do not be bashful about letting other people know that you are looking for work. Classmates, friends, and business associates of your family may be of help not only directly but also indirectly, acting as extra pairs of eyes and ears alert to job opportunities for you.

Planning Your Approach (the Preapproach)

After conducting your self-analysis and identifying potential employers looking for people with your abilities and interests, you need to prepare your résumé (or personal advertisement). Your résumé should focus on your achievements to date, your educational background, your work experience, and your special abilities and interests. Some students make the mistake of merely listing their assigned responsibilities on different jobs without indicating what they accomplished on the job. If you achieved something on the job, say it—for example, "Helped computerize office files," "Increased sales in my territory by 10 percent," "Received a 15 percent raise after three months on the job," or "Promoted to assistant store manager after four months." When looking for a job, remember that employers are looking for a track record of achievement, so you must distinguish yourself from those who may have had the same assigned job responsibilities as you did but performed poorly. If your work experience is minimal, consider a "skills" résumé, in which you emphasize your particular abilities, such as organizing, programming, or leadership skills, and give supporting evidence whenever you can. Examples of various types of résumés can be found in the *College Placement Annual* and in various other job-hunting publications (ask your college business reference librarian to direct you). Exhibit 2 lists some Web sites where you can learn about résumé formats.

Remember that there is no one correct format for your résumé. A little tasteful creativity can help differentiate your résumé from countless look-alike résumés. If you are a young college graduate, your résumé will usually be only one page long, but do not worry about going to a second page if you have something important to present. One student so blindly followed the one-page résumé rule that he left out having served in the military—service that is usually viewed very positively by prospective employers, especially

Exhibit 3
Sample Résumé

RACHEL E. SANFORD
2935 Mountain View Road
Ellington, PA 19401
(216) 567-0000

JOB OBJECTIVE	Sales representative for a consumer-products company
EDUCATION	Graduated *cum laude* with BS in Marketing Management (June 2006), University of Southern Pennsylvania. Career-related courses included Selling and Sales Management, Public Speaking, Business Writing, Public Relations, Marketing Research, Computer Programming, and Multivariate Data Analysis.
ACTIVITIES AND HONORS	President, Student Marketing Association; Vice president, Chi Omega Sorority; Captain, women's varsity tennis team; sportswriter for the *Campus View* student newspaper. Named to Who's Who among American College Students, 2004–2005. On Dean's List all four years. Overall grade point average = 3.65.
WORK EXPERIENCE	
Summer 2005	*Sales representative,* Peabody Manufacturing Company. Sold women's blouses to boutiques and small department stores in southeastern Pennsylvania. Exceeded assigned sales quota by 20 percent; named "outstanding" summer employee for 2005.
Summer 2004	*Buyer,* Hamm's Department Stores, Inc., Midway, Pa. Developed purchase plan, initiated purchase orders, monitored and controlled expenditures for nearly $2 million worth of women's clothing. Made monthly progress reports (written and oral) to Hamm's Executive Committee. Received 15 percent bonus as #2 buyer in the six stores of the Hamm's chain in special "Back to School" purchasing competition.
Summer 2003	*Retail clerk,* Hamm's Department Stores, Inc., Midway, Pa. After 3 months, received 10 percent pay raise and promotion to evening salesclerk supervisor over seven part-time salesclerks. Devised new inventory control system for handbags and accessories that cut costs over $50,000 annually.
Summer 2002	*Cosmetics salesperson,* Heavenly Charm, Inc., Midway, Pa. Sold $63,000 worth of Heavenly Charm cosmetics door to door. Named #1 salesperson in the sales region. Offered full-time job as sales supervisor.
INTERESTS	Tennis, golf, public speaking, short story writing, and reading biographies.

if it involved significant leadership responsibilities or work experience.

If you know what job you want, you may want to put your job objective near the top of your résumé. If you are not sure what job you want or want to send out the same résumé for several different jobs, then you can describe your job objective in your cover letter. A key element in the cover letter is convincing the prospective employer to grant you an interview. Thus, you must talk in terms of the employer's interests, not just your own. You are answering the question: "Why should we hire you?" You may need to send a letter with your résumé enclosed to a hundred or more companies to obtain five to ten interviews, so do not be discouraged if you get replies from only a few companies or are told by many companies that they have no job opportunities at present. You will probably need only a few interviews and just one job offer to get your career started.

Review some of the publications and sources mentioned in the previous section on prospecting (e.g., *College Placement Annual,* Dun and Bradstreet directories, and annual reports) to learn as much as you can about your prospective employer so that you can tailor your cover letter. Remember, the employer is thinking in terms of the company's needs, not yours. For one example of a résumé, see Exhibit 3. A cover letter is illustrated in Exhibit 4.

Making Your Approach

Prospective employers can be approached by mail, telephone, the Internet, or personal contact. Personal contact is best, but this usually requires that you know someone with influence who can arrange an interview for you. Of course, a few enterprising students have devised elaborate and sometimes successful schemes to get job interviews. For example, we know of one young man who simply went to the headquarters of the company he wanted to work for and asked to see the president. Told that the president of the company could not see him, the student said that he was willing to wait until the president had time. This audacious individual went back three different days until the president finally agreed to see him, perhaps mainly out of curiosity about what sort of young man would be so outrageous in his job search.

Fortunately for this young man, he had a lot to offer and was able to communicate this to the president, so he was hired. This unorthodox approach shows how far people have gone to impress potential employers, and if you feel comfortable doing it, then go ahead. A personal contact within the company certainly can win you some special attention and enable you to avoid competing head-on with the large number of other candidates looking for a job. Most students, however, start their approach in the traditional way by

Exhibit 4

Sample Cover Letter

Rachel E. Sanford
2935 Mountain View Road
Ellington, PA 19401

Mr. Samuel Abramson
District Sales Manager
Hixson Appliance Company
Philadelphia, PA 19103

Dear Mr. Abramson:

Hixson has been a familiar name to me ever since I was barely able to see over my mother's kitchen counter. Virtually every appliance we had was a Hixson, so I know firsthand what fine quality products you sell. My career interest is in sales, and there is no company that I would rather work with than Hixson Appliance.

I will be graduating this June from Southern Pennsylvania University with a BS in marketing management, and I would like you to consider me for a job as a sales representative with your company. As you can see in my enclosed résumé, I have successfully worked in sales jobs during three of the last four summers. My college course electives (e.g., public speaking, business writing, and public relations) have been carefully selected with my career objective in mind. Even my extracurricular activities in sports and campus organizations have helped prepare me for working with a variety of people and competitive challenges.

Will you please grant me an interview so that I can convince you that I'm someone you should hire for your sales team? I'll call you next Thursday afternoon to arrange an appointment at your convenience.

Look forward to meeting you soon.

Sincerely,
Rachel E. Sanford
Enclosure

mailing their résumé and cover letter to the recruiting department of the company. More recently, students have begun to e-mail their résumés, and some companies are requiring this as a means of screening out applicants who are not computer literate. Unless your résumé matches a particular need at that time, it will probably be filed away for possible future reference or merely discarded. To try to get around the system, some students send their letter by express mail or mailgram or address it to a key executive, with "Personal" written on the envelope. These students believe that bypassing the company's personnel office will increase the likelihood that their cover letter and résumé will be read by someone with authority to hire. Other students send their résumé on a CD or DVD, and one student in Louisiana sent a King Cake to the recipient of the résumé, while another sent a packet of Louisiana spices. Using gimmicks, no matter how creative, to get a job interview will offend some executives and thus cause you to be rejected from consideration for a job. But you can probably also be sure that a few executives will admire your efforts and grant you an interview.

Only you know how comfortable you feel with different approaches to obtaining a job interview. We advise you not to use an approach that is out of character for you and thus will make you feel awkward and embarrassed.

Making Your Sales Presentation

Your personal sales presentation will come during the interview with the prospective employer's recruiters or interviewers. Like any presentation, it requires thorough preparation and an effective follow-up, as well as a solid performance during the interview itself.

Pre-Interview Considerations

Preparing for the interview is crucial. You will already have gathered information on the company, as suggested in the preceding sections; you should review it now. Exhibit 5 shows a pre-interview checklist that can help you prepare. In addition, the self-assessment test in Exhibit 6 can help you determine if you're ready for the interview.

Keep the following in mind in preparing for your interview:

- Find out the exact place and time of the interview.
- Be certain you know the interviewer's name and how to pronounce it if it looks difficult.
- Do some research on the company with which you are interviewing—talk to people and read the company literature to know what its products or services are, where its offices are located, what its growth has been, and how its prospects look for the future.
- Think of two or three good questions that you would like to ask during your interview.

Exhibit 5
Before the Interview

- **Practice**
  - ✓ Questions you may be asked
  - ✓ Questions you want to ask about the position and organization
  - ✓ Role-playing an interview
- **Self-assessment**
  - ✓ Goals
  - ✓ Skills, abilities, accomplishments
  - ✓ Work values (important factors you look for in a job)
  - ✓ Experiences
  - ✓ Personality
- **Research**
  - ✓ Obtain company literature
  - ✓ Write or visit the organization
  - ✓ Talk to people familiar with the organization
- **Obtain references**
- **Plan ahead**
  - ✓ Attire to be worn to the interview
  - ✓ Directions to the interview site
  - ✓ Time of arrival (get there with at least 5–10 minutes to spare)

- Plan to arrive at the designated place for your interview a little early so that you will not feel rushed and worried about being on time.
- Plan to dress in a manner appropriate to the job for which you are interviewing.

A guide for the interview conversation itself is to prepare nine positive thoughts before you go in for the interview:

- Three reasons why you selected the employer to interview
- Three reasons you particularly like the employer
- Three assets you have that should interest the employer

Try to make a positive impression on everyone you encounter in the company, even while waiting in the lobby for your interview. Sometimes managers will ask their receptionists and secretaries for an opinion of you, and your friendliness, courtesy, professional demeanor, personal habits, and the like will all be used to judge you. Even the magazines you choose to read while waiting can be a positive or negative factor. For instance, it will probably be less impressive if you leaf through a popular magazine like *People or Sports*

Exhibit 6

Self-Assessment Test

How assertive are you (or will you be) as you interview for a position? Listed below are questions that will help you to evaluate yourself: answer yes or no to the questions, being honest with yourself. If you have five or fewer yes answers, you still have some work to do. A good score is seven or more yes answers.

Yes	No	
——	——	Have you made an effort to research the company before the interview?
——	——	Have you prepared several questions that you want to ask?
——	——	If an interviewer asks a personal question unrelated to the job, will you be able to tactfully call this to his attention?
——	——	If an interviewer gives you a hypothetical job-related problem, do you have confidence in your ability to respond in a timely and succinct manner?
——	——	If the interviewer seems distracted or uninterested during your interview, will you be able to steer the interview back on track and gain her attention?
——	——	When you meet the interviewer, will you be the first to introduce yourself and begin the conversation?
——	——	If the interviewer continually interrupts when you are responding to questions or giving information about yourself, can you politely handle this?
——	——	If the interviewer never gives you the opportunity to talk about yourself and you have only five minutes remaining in the interview, have you thought about phrases or ways to redirect the interview and regain control of the process?
——	——	When the interviewer is beginning to close the interview, are you prepared to ask questions about how you stand, what the determining factors are for candidate selection, and by what date you will have an answer?

Illustrated than if you read something more professional such as *Business Week* or *The Wall Street Journal*.

During the Interview

During the interview, do not be merely a passive respondent to the interviewer's questions. Being graciously assertive by asking reasonable questions of your own will indicate to the interviewer that you are alert, energetic, and sincerely interested in the job. The personal interview is your opportunity to persuade the prospective employer that you should be hired. To use a show business analogy, you will be onstage for only a short time (during the personal interview), so try to present an honest but positive image of yourself. Perhaps it will help you to be alert and enthusiastic if you imagine that you are being interviewed on television. Exhibit 7 lists a number of questions that are frequently asked during interviews.

Sometimes prospective employers will ask you to demonstrate certain abilities by having you write a timed essay about some part of your life, sell something (such as a desk calculator) to the interviewer, or respond to hostile questions. Be calm and confident during any such unorthodox interviewing approaches and you will make a good impression. Remember, most employers want you to perform well because they are looking for the best people they can find in a given time frame for the money they have to offer.

If you are given intelligence, aptitude, or psychological tests, you should try to be honest so that you do not create unrealistic expectations that you will not be able to fulfill. It is just as important that you do not create a false impression and begin with a company that is not right for you as it is to secure employment in the first place. Many experts say that it is not very difficult to "cheat" on aptitude or psychological tests if you are able to "play the role" and provide the answers that you know the company wants to read. Usually, the so-called safe approach in most personality and preference (interest) tests is to not take extreme positions on anything that is not clearly associated with the job you are applying for. For sales jobs, it is probably safe to come across as highly extroverted and interested in group activities, but it may not be safe to appear to be overly interested in literature, music, art, or any solitary activity. In addition, the "right" answers tend to indicate a conservative, goal-oriented, money-motivated, and gregarious personality.

Dealing with Objections. Sometimes interviewers will bluntly ask, "Why should we hire you?" This requires that you think in terms of the employer's needs and present in concise form all your major "selling points." Also, sometimes the interviewer may bring up reasons why you are not the ideal candidate. For example, he or she may say: (1) "We're really looking

Exhibit 7

Some Questions Frequently Asked During a Job Interview

- Of the jobs you've had to date, which one did you like best? Why?
- Why do you want to work for our company?
- Tell me what you know about our company.
- Do any of your relatives or friends work for our company? If so, in what jobs?
- Tell me about yourself, your strengths, weaknesses, career goals, and so forth.
- Is any member of your family a professional marketer? If so, what area of marketing?
- Why do you want to start your career in marketing?
- Persuade me that we should hire you.
- What extracurricular activities did you participate in at college? What leadership positions did you have in any of these activities?
- What benefits have you derived from participation in extracurricular activities that will help you in your career?
- Where do you see yourself within our company in five years? In ten years? Twenty years?
- What is your ultimate career goal?
- What do you consider your greatest achievement to date?
- What is your biggest failure to date?
- What is (was) your favorite subject in school? Why?
- Are you willing to travel and possibly relocate?
- How would the people who know you describe you?
- How would you describe yourself?
- What do you like most about marketing?
- What do you like least about marketing?
- If we hire you, how soon could you start work?
- What is the minimum we would have to offer you to come with us?
- What goals have you set for yourself? How are you planning to achieve them?
- Who or what has had the greatest influence on the development of your career interests?
- What factors did you consider in choosing your major?
- Why are you interested in our organization?
- What can you tell me about yourself?
- What two or three things are most important to you in a position?
- What kind of work do you want to do?
- What can you tell me about a project you initiated?
- What are your expectations of your future employer?
- What is your GPA? How do you feel about it? Does it reflect your ability?
- How do you resolve conflicts?
- What do you feel are your strengths? Your weaknesses? How do you evaluate yourself?
- What work experience has been the most valuable to you and why?
- What was the most useful criticism you ever received, and who was it from?
- Can you give an example of a problem you have solved and the process you used?
- Can you describe the project or situation that best demonstrates your analytical skills?
- What has been your greatest challenge?
- Can you describe a situation where you had a conflict with another individual and explain how you dealt with it?
- What are the biggest problems you encountered in college? How did you handle them? What did you learn from them?
- What are your team-player qualities? Give examples.
- Can you describe your leadership style?
- What interests or concerns you about the position or the company?
- In a particular leadership role you had, what was the greatest challenge?
- What idea have you developed and implemented that was particularly creative or innovative?
- What characteristics do you think are important for this position?

Exhibit 7

Some Questions Frequently Asked During a Job Interview (continued)

- How have your educational and work experiences prepared you for this position?
- Can you take me through a project where you demonstrated skills?
- How do you think you have changed personally since you started college?
- Can you tell me about a team project that you are particularly proud of and discuss your contribution?
- How do you motivate people?
- Why did you choose the extracurricular activities you did? What did you gain? What did you contribute?
- What types of situations put you under pressure, and how do you deal with the pressure?
- Can you tell me about a difficult decision you have made?
- Can you give an example of a situation in which you failed and explain how you handled it?
- Can you tell me about a situation when you had to persuade another person of your point of view?
- What frustrates you the most?
- Knowing what you know now about your college experience, would you make the same decisions?
- What can you contribute to this company?
- How would you react to having your credibility questioned?
- What characteristics are important in a good manager? How have you displayed one of these characteristics?
- What challenges are you looking for in a position?
- What two or three accomplishments have given you the most satisfaction?
- Can you describe a leadership role of yours and tell why you committed your time to it?
- How are you conducting your job search, and how will you make your decision?
- What is the most important lesson you have learned in or out of school?
- Can you describe a situation where you had to work with someone who was difficult? How was the person difficult, and how did you handle it?
- We are looking at a lot of great candidates; why are you the best person for this position?
- How would your friends describe you? Your professors?
- What else should I know about you?

for someone with a little more experience"; (2) "We'd like to get someone with a more technical educational background"; or (3) "We need someone to start work within two weeks." These kinds of statements are similar to objections or requests for additional information. In other words, the interviewer is saying, "Convince me that I shouldn't rule you out for this reason." To overcome such objections, you might respond to each, respectively, along the following lines:

(1) "I've had over a year's experience working with two different companies during my summer vacations, and I've worked part-time with a third company all during college. I'm a fast learner, and I've adapted well to each of the three companies, so I feel that my working experience is equivalent to that of someone who has had three or four years' experience with the same company."

(2) "Although I didn't choose to earn a technical undergraduate degree, I've taken several technical courses in college, including basic engineering courses, chemistry, physics, and two years of math. I'm very confident that I can quickly learn whatever is necessary technically to do the job, and my real strength is that my education has been a blend of technical and managerial courses."

(3) "Well, I do have one more term of school, so I couldn't start full-time work in two weeks, but perhaps we could work out an arrangement in which I could work part-time—maybe Friday, Saturday, and Sunday or on weekends until I graduate."

Good "salespeople" do not allow an objection to block a sale. Providing reasonable solutions or alternative perspectives can often overcome objections or, at least, allow room for further negotiation toward a compromise solution.

How to Act during the Interview. The following can help you behave appropriately during the interview:

- Think positive. Be enthusiastic, interested, knowledgeable, and confident.
- Take few notes. It is acceptable to take notes during the interview, but limit them to things that are essential to remember. You want to focus more on listening and observing rather than writing.

Exhibit 8

Sample Interview Questions to Be Asked by Job Candidates

- Where is the organization going? What plans or projects are being developed to maintain or increase its market share? Have many new product lines been decided upon recently? Is the sales growth in the new product line sustainable?
- Who are the people with whom I will be working? May I speak with some of them?
- May I have a copy of the job description?
- What might be a typical first assignment?
- Do you have a performance appraisal system? How is it structured? How frequently will I be evaluated?
- What is the potential for promotion in the organization? In promotions, are employees ever transferred between functional fields? What is the average time to get to ——— level in the career path? Is your policy to promote from within, or are many senior jobs filled by experienced people from outside? Do you have a job posting system?
- What type of training will I receive? When does the training program begin? Is it possible to move through your program faster? About how many individuals go through your internship program?
- What is the normal routine of a (an) ——— like? Can I progress at my own pace, or is it structured? Do employees normally work overtime?
- How much travel is normally expected? Is a car provided to traveling personnel?
- How much freedom is given to new people? How much discipline is required? How much input does the new person have? How much decision-making authority is given to new personnel?
- How frequently do you relocate employees? Is it possible to transfer from one division to another?
- What is the housing market for a single person in ——— (city)? Is public transportation adequate?
- How much contact with and exposure to management is there?
- How soon should I expect to report to work?

- Relate to the interviewer. Build positive rapport with the interviewer. Listen and observe; relate yourself to the employer or position.
- Watch your body language. Be aware of nervousness (fidgeting, shaking leg, tapping, etc.). Project confidence (eye contact, firm handshake, upright posture).
- Be aware of the questions the employer asks. Answer with information relevant to the position. Provide a direct answer; avoid being long-winded.
- Think about the questions you ask. They should indicate that you know something about the job. Avoid questions that could easily be answered elsewhere (through research). Obtain information you need to know to be satisfied with the job (interviewing is a two-way process). Salary and benefit questions should be asked after the job is offered.
- Achieve effective closure. Ask when the employer expects to make a decision. Restate your interest and ability to perform the job. Show confidence and enthusiasm (smile, end with a firm handshake). Obtain the employer's business card, if possible (it may be useful when writing a thank-you letter).

Interview Questions. Too many employment applicants spend all their time preparing for the questions employers will ask them. Too often, they fail to ask vital questions that would help them learn if a job is right for them. Failing to ask important questions during the interview often leads to jobs that offer neither interest nor challenge. Too often, uninformed applicants accept positions hoping that they will develop into something more meaningful and rewarding later. Exhibit 8 suggests questions that you may want to ask.

Closing the Sale

Although it is not likely that a prospective employer will offer you a job immediately after the job interview, you should nevertheless let the interviewer know that you definitely want the job and are confident that you will do an excellent job for the employer. You will need to use your best judgment on how to best do this.

In each stage of the personal selling process, you should be looking for feedback from the interviewer's body language and voice inflections or tone.

Following Up the Interview

Within a few days after any job interview, whether you want the job or not, it is business courtesy to write thank-you letters to interviewers. In these letters you can reinforce the positive impression you made in the interview and again express your keen interest in working for the company. If you do not hear from the company within a few weeks, it may be appropriate to write another letter expressing your continuing interest in the job and asking for a decision so that you can consider other options if necessary. As a possible reason for this follow-up letter, you might mention an additional personal achievement since the interview, give a more detailed answer to one of the interviewer's questions, or perhaps send a newspaper or magazine article of interest. A neat, well-written, courteous follow-up letter gives you a chance not only to make a stronger impression on the interviewer but also to exhibit positive qualities such as initiative, energy, sensitivity to others' feelings, and awareness of business protocol.

Many applicants fail to write a thank-you letter after an interview, yet many employers say that the deciding factor between several similar job candidates is often the thank-you note. The thank-you letter should be typewritten. If the interviewer is a very technology-driven person, a thank-you e-mail may also be appropriate. However, the personal touch of a typewritten and hand-signed letter leaves a better impression.

Be sure to write a follow-up letter in all of the following situations:

- After two or three weeks of no reply.
- When a job has been refused. Express your regret that no job is available and ask if you might be considered in the future. Also, ask how you could improve yourself to better fit what the company is looking for.
- After an interview. Express your thanks for the interviewer's time and courtesy. Answer any unanswered questions and clarify any misconceptions.
- To accept a job (even if previously done in person or on the phone). State your acceptance. Reiterate the agreement, the time for beginning work, and the like. Do not start asking for favors.
- To refuse a job offer. Graciously decline the offer. Be warm and interested and indicate that you appreciate the offer.

Follow-up letters are also appropriate after you have received replies to both solicited and unsolicited letters of inquiry. Always make certain that your letters possess the attitude, quality, and skill of a professional.

ON THE JOB

Working Conditions

Advertising, marketing, promotions, public relations, and sales managers work in offices close to those of top managers. Long hours, including evenings and weekends, are common. About 44 percent of advertising, marketing, and public relations managers work more than 40 hours per week. Substantial travel may also be involved. For example, attendance at meetings sponsored by associations or industries is often mandatory. Sales managers travel to local, regional, and national offices and to various dealers and distributors. Advertising and promotions managers may travel to meet with clients or representatives of communications media. At times, public relations managers travel to meet with special interest groups or government officials. Job transfers between headquarters and regional offices are common, particularly among sales managers.

Moving Up the Ladder

Most advertising, marketing, promotions, public relations, and sales management positions are filled by promoting experienced staff or related professional personnel. For example, many managers are former sales representatives, purchasing agents, buyers, or product, advertising, promotions, or public relations specialists. In small firms, where the number of positions is limited, advancement to a management position usually comes slowly. In large firms, promotion may occur more quickly.

Although experience, ability, and leadership are emphasized for promotion, advancement can be accelerated by participation in management training programs conducted by many large firms. Many firms also provide their employees with continuing education opportunities, either in-house or at local colleges and universities, and encourage employee participation in seminars and conferences, often provided by professional societies. In collaboration with colleges and universities, numerous marketing and related associations sponsor national or local management training programs. Staying abreast of what is happening in your industry and getting involved in related industry associations can be important for your career advancement.

YOUR EARLY WORKING CAREER

Even though you want to choose a company that you will stay with throughout your working life, it is realistic to recognize that you will probably work for three, four, or more companies during your career. If you are not fully satisfied with your job or company during the first few years of your full-time working life, remember that you are building experience and knowledge that will increase your marketability for future job opportunities. Keep a positive outlook and do the best you can in all job assignments—and your chance for new opportunities will come. Do not be too discouraged by mistakes that you may make in your career; nearly every successful person has made and continues to make many mistakes. View these mistakes largely as learning experiences, and they will not be too traumatic or damaging to your confidence.

Good luck in your marketing career!

CHAPTER

2

Strategic Planning for Competitive Advantage

Learning Outcomes

LO 1 Understand the importance of strategic marketing and know a basic outline for a marketing plan

LO 2 Develop an appropriate business mission statement

LO 3 Describe the components of a situation analysis

LO 4 Explain the criteria for stating good marketing objectives

LO 5 Identify sources of competitive advantage

LO 6 Identify strategic alternatives

LO 7 Discuss target market strategies

LO 8 Describe the elements of the marketing mix

LO 9 Explain why implementation, evaluation, and control of the marketing plan are necessary

LO 10 Identify several techniques that help make strategic planning effective

LO 1

The Nature of Strategic Planning

Strategic planning is the managerial process of creating and maintaining a fit between the organization's objectives and resources and the evolving market opportunities. The goal of strategic planning is long-run profitability and growth. Thus, strategic decisions require long-term commitments of resources.

A strategic error can threaten a firm's survival. On the other hand, a good strategic plan can help protect and grow the firm's resources. For instance, if the March of Dimes had decided to focus on fighting polio, the organization would no longer exist. Most of us view polio as a conquered disease. The March of Dimes survived by making the strategic decision to switch to fighting birth defects.

Strategic marketing management addresses two questions: What is the organization's main activity at a particular time? How will it reach its goals? Here are some examples of strategic decisions:

- The decision of Sears to buy Lands' End, a successful clothing catalog and online retail business. The move could upgrade Sears' image and increase its presence in the catalog business and on the Internet. Lands' End clothing will enjoy greater retail distribution in Sears stores.
- Hewlett-Packard's decision to stop competing head on with Dell in selling computers on the Internet and phone, and focus on its strength, retail stores, where Dell had no presence at all.[1]
- McDonald's decision to offer more healthful foods by focusing on fresh fruits and vegetables with its new line of premium salads.[2]
- S. C. Johnson's introduction of Shout Color Catchers, a laundry sheet for the washer that collects loose dyes and prevents clothes from bleeding color onto other laundry items.

All these decisions have affected or will affect each organization's long-run course, its allocation of resources, and ultimately its financial success. In contrast, an operating decision, such as changing the package design for Post's cornflakes or altering the sweetness of a Kraft salad dressing, probably won't have a big impact on the long-run profitability of the company.

How do companies go about strategic marketing planning? How do employees know how to implement the long-term goals of the firm? The answer is a marketing plan.

strategic planning
The managerial process of creating and maintaining a fit between the organization's objectives and resources and evolving market opportunities.

planning
The process of anticipating future events and determining strategies to achieve organizational objectives in the future.

Marketing & You

What do you think about planning? Enter your answers on the lines provided.

Describes my style

1	2	3	4	5	6	7
Not at all						Perfectly

— I start my work without spending too much time on planning.*

— I list the steps necessary for completing a task before starting it.

— I think about strategies I will fall back on if problems arise.

— Because so many aspects of my work are unpredictable, planning is not useful.*

— I keep good records of the projects I'm working on.

— I set personal goals for myself.

— Each week I make a plan for what I need to do.

— I do not waste time thinking about what I should do.*

— I am careful to work on the highest-priority tasks first.

— Planning is a waste of time.*

— Planning is an excuse for not working.*

— I don't need to develop a strategy for completing my assignments.*

Now, total your score, reversing your score for items with asterisks—that is, if you put a 2, put a 6, and vice versa. Read the chapter, and see what your score means at the end.

WHAT IS A MARKETING PLAN?

marketing planning
Designing activities relating to marketing objectives and the changing marketing environment.

marketing plan
A written document that acts as a guidebook of marketing activities for the marketing manager.

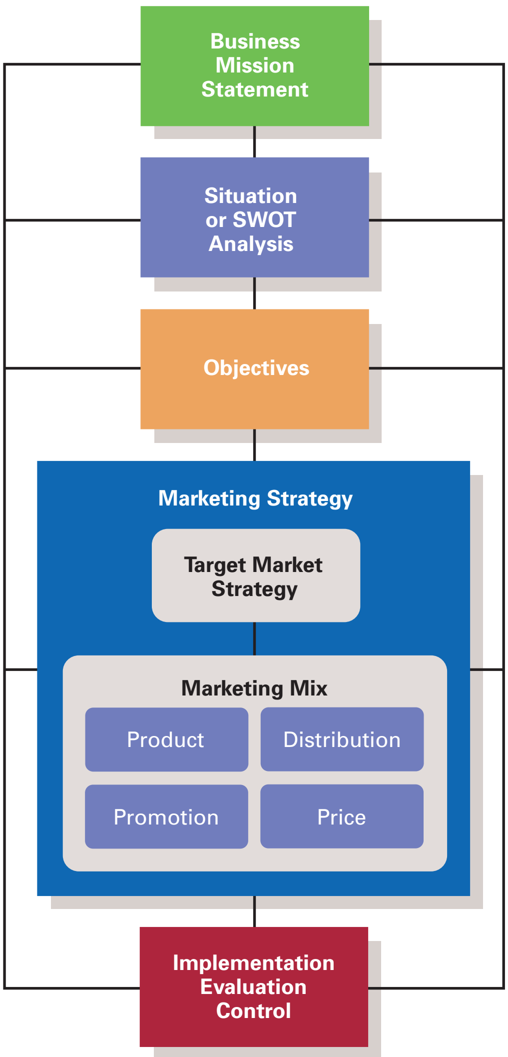
Planning is the process of anticipating future events and determining strategies to achieve organizational objectives in the future. Marketing planning involves designing activities relating to marketing objectives and the changing marketing environment. Marketing planning is the basis for all marketing strategies and decisions. Issues such as product lines, distribution channels, marketing communications, and pricing are all delineated in the marketing plan. The marketing plan is a written document that acts as a guidebook of marketing activities for the marketing manager. In this chapter, you will learn the importance of writing a marketing plan and the types of information contained in a marketing plan.

Why Write a Marketing Plan?

By specifying objectives and defining the actions required to attain them, a marketing plan provides the basis by which actual and expected performance can be compared. Marketing can be one of the most expensive and complicated business activities, but it is also one of the most important. The written marketing plan provides clearly stated activities that help employees and managers understand and work toward common goals.

Writing a marketing plan allows you to examine the marketing environment in conjunction with the inner workings of the business. Once the marketing plan is written, it serves as a reference point for the success of future activities. Finally, the marketing plan allows the marketing manager to enter the marketplace with an awareness of possibilities and problems.

Exhibit 2.1
Elements of a Marketing Plan



Marketing Plan Elements

Marketing plans can be presented in many different ways. Most businesses need a written marketing plan because a marketing plan is large and can be complex. Details about tasks and activity assignments may be lost if communicated orally. Regardless of the way a marketing plan is presented, some elements are common to all marketing plans. These include defining the business mission, performing a situation analysis, defining objectives, delineating a target market, and establishing components of the marketing mix. Exhibit 2.1 shows these elements, which are also described further below. Other elements that may be included in a plan are budgets, implementation timetables, required marketing research efforts, or elements of advanced strategic planning. An example of a marketing plan appears in the appendix to this chapter.

Selecting which alternative to pursue depends on the overall company philosophy and culture. The choice also depends on the tool used to make the decision. Companies generally have one of two philosophies about when they expect profits. They either pursue profits right away or first seek to increase market share and then pursue profits. In the long run, market share and profitability are compatible goals. Many companies have long followed this credo: Build market share, and profits will surely follow. Michelin, the tire producer, consistently sacrifices short-term profits to achieve market share. On the other hand, IBM stresses profitability and stock valuation over market share, quality, and customer service. As you can see, the same strategic alternative may be viewed entirely differently by different firms.

A number of tools exist to help managers select a strategic alternative. The most common of these tools are in matrix form. The portfolio matrix is described here in more detail.

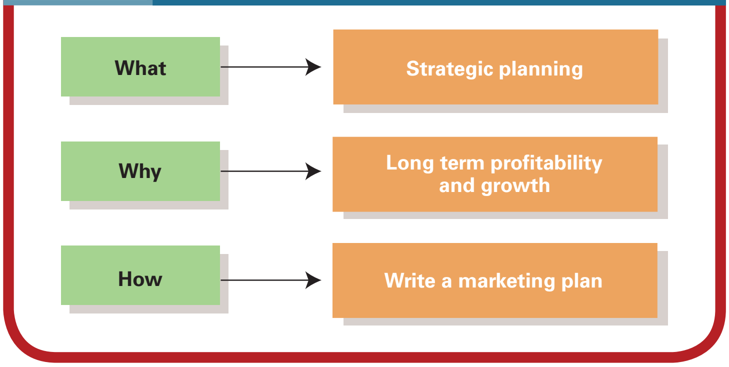
WRITING THE MARKETING PLAN

The creation and implementation of a complete marketing plan will allow the organization to achieve marketing objectives and succeed. However, the marketing plan is only as good as the information it contains and the effort, creativity, and thought that went into its creation. Having a good marketing information system and a wealth of competitive intelligence (covered in Chapter 9) is critical to a thorough and accurate situation analysis. The role of managerial intuition is also important in the creation and selection of marketing strategies. Managers must weigh any information against its accuracy and their own judgment when making a marketing decision.

Note that the overall structure of the marketing plan (Exhibit 2.1) should not be viewed as a series of sequential planning steps. Many of the marketing plan elements are decided on simultaneously and in conjunction with one another. Further, every marketing plan has a different content, depending on the organization, its mission, objectives, targets, and marketing mix components. The example of a marketing plan in the chapter appendix should not be regarded as the only correct format for a marketing plan. Many organizations have their own distinctive format or terminology for creating a marketing plan. Every marketing plan should be unique to the firm for which it was created. Remember, however, that although the format and order of presentation should be flexible, the same types of questions and topic areas should be covered in any marketing plan. As you can see by the extent of the marketing plan in the appendix, creating a complete marketing plan is not a simple or quick effort.

REVIEW LEARNING OUTCOME

LO 1 Understand the importance of strategic marketing and know a basic outline for a marketing plan



LO 2
Defining the Business Mission

mission statement
A statement of the firm's business based on a careful analysis of benefits sought by present and potential customers and an analysis of existing and anticipated environmental conditions.

The foundation of any marketing plan is the firm's **mission statement,** which answers the question, "What business are we in?" The way a firm defines its business mission profoundly affects the firm's long-run resource allocation, profitability, and survival. The mission statement is based on a careful analysis of benefits sought by present and potential customers and an analysis of existing and anticipated environmental conditions. The firm's mission statement establishes boundaries for all subsequent decisions, objectives, and strategies. The Southwest Airlines mission statement is shown in Exhibit 2.2.

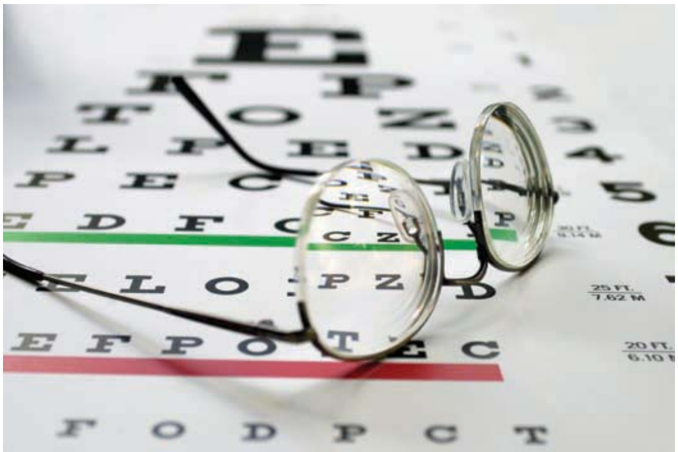
Exhibit 2.2
Southwest Airlines Mission Statement

The mission of Southwest Airlines is dedication to the highest quality of Customer Service delivered with a sense of warmth, friendliness, individual pride, and Company Spirit.

To Our Employees

We are committed to provide our Employees a stable work environment with equal opportunity for learning and personal growth. Creativity and innovation are encouraged for improving the effectiveness of Southwest Airlines. Above all, Employees will be provided the same concern, respect, and caring attitude within the organization that they are expected to share externally with every Southwest Customer.

SOURCE: http://www.southwestairlines.com/about_swa/mission



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A mission statement should focus on the market or markets the organization is attempting to serve rather than on the good or service offered. Otherwise, a new technology may quickly make the good or service obsolete and the mission statement irrelevant to company functions. Business mission statements that are stated too narrowly suffer from marketing myopia—defining a business in terms of goods and services rather than in terms of the benefits customers seek. In this context, *myopia* means narrow, short-term thinking. For example, Frito-Lay defines its mission as being in the snack-food business rather than in the corn chip business. The mission of sports teams is not just to play games but to serve the interests of the fans.

Alternatively, business missions may be stated too broadly. "To provide products of superior quality and value that improve the lives of the world's consumers" is probably too broad a mission statement for any firm except Procter & Gamble. Care must be taken when stating what business a firm is in. For example, the mission of Ben & Jerry's centers on three important aspects of its ice cream business: (1) Product: "To make, distribute and sell the finest quality all natural ice cream and related products in a wide variety of innovative flavors made from Vermont Dairy products; " (2) Economic: "To operate the company on a sound financial basis of profitable growth, increasing value for our shareholders, and creating career opportunities and financial rewards for our employees;" and (3) Social: "To operate the company in a way that actively recognizes the central role that business plays in the structure of society by initiating innovative ways to improve the quality of life of a broad community—local, national, and international."[3] By correctly stating the business mission in terms of the benefits that customers seek, the foundation for the marketing plan is set. Many companies are focusing on designing more appropriate mission statements because these statements are frequently displayed on the company's Web sites.

marketing myopia
Defining a business in terms of goods and services rather than in terms of the benefits that customers seek.

strategic business unit (SBU)
A subgroup of a single business or a collection of related businesses within the larger organization.

REVIEW LEARNING OUTCOME

LO 2 Develop an appropriate business mission statement

Q: What business are we in?

A: Business mission statement

- Too narrow → marketing myopia
- Too broad → no direction
- Just right → focus on markets served and benefits customers seek

The organization may need to define a mission statement and objectives for a strategic business unit (SBU), which is a subgroup of a single business or a collection of related businesses within the larger organization. A properly defined SBU should have a distinct mission and specific target market, control over its resources, its own competitors, and plans independent of the other SBUs in the organization. Thus, a large firm such as Kraft Foods may have marketing plans for each of its SBUs, which include breakfast foods, desserts, pet foods, and beverages.

LO 3 Conducting a Situation Analysis

Marketers must understand the current and potential environment that the product or service will be marketed in. A situation analysis is sometimes referred to as a SWOT analysis; that is, the firm should identify its internal strengths (S) and weaknesses (W) and also examine external opportunities (O) and threats (T).

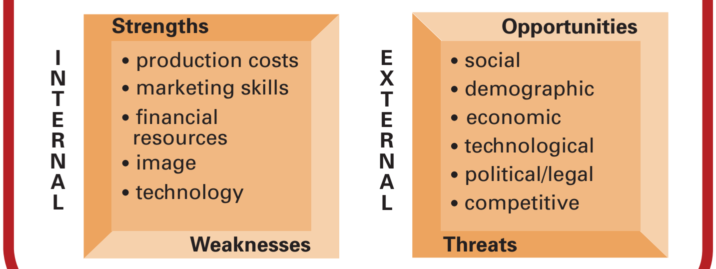
SWOT analysis
Identifying internal strengths (S) and weaknesses (W) and also examining external opportunities (O) and threats (T).

When examining internal strengths and weaknesses, the marketing manager should focus on organizational resources such as production costs, marketing skills, financial resources, company or brand image, employee capabilities, and available technology. For example, a potential weakness for AirTran Airways (formerly ValuJet) is the age of its airplane fleet, which could project an image of danger or low quality. Other weaknesses include high labor turnover rates and limited flights. A potential strength is the airline's low operating costs, which translate into lower prices for consumers. Another issue to consider in this section of the marketing plan is the historical background of the firm—its sales and profit history.

When examining external opportunities and threats, marketing managers must analyze aspects of the marketing environment. This process is called environmental scanning—the collection and interpretation of information about forces, events, and relationships in the external environment that may affect the future of the organization or the implementation of the marketing plan. Environmental scanning helps identify market opportunities and threats and provides guidelines for the design of marketing strategy. The six most often studied macroenvironmental forces are social, demographic, economic, technological, political and legal, and competitive. These forces are examined in detail in Chapter 3. For example, H&R Block, a tax preparation service, benefits from complex changes in the tax codes that motivate citizens to have their tax returns prepared by a professional. Alternatively, tax-simplification or flat-tax plans would allow people to easily prepare their own returns.

REVIEW LEARNING OUTCOME

LO 3 Explain the components of a situation analysis



LO 4 Setting Marketing Plan Objectives

environmental scanning
Collection and interpretation of information about forces, events, and relationships in the external environment that may affect the future of the organization or the implementation of the marketing plan.

marketing objective
A statement of what is to be accomplished through marketing activities.

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Before the details of a marketing plan can be developed, objectives for the plan must be stated. Without objectives, there is no basis for measuring the success of marketing plan activities.

A marketing objective is a statement of what is to be accomplished through marketing activities. To be useful, stated objectives should meet several criteria:

- *Realistic*: Managers should develop objectives that have a chance of being met. For example, it may be unrealistic for start-up firms or new products to command dominant market share, given other competitors in the marketplace.
- *Measurable*: Managers need to be able to quantitatively measure whether or not an objective has been met. For example, it would be difficult to determine success for an objective that states "To increase sales of cat food." If the company sells 1 percent more cat food, does that mean the objective was met? Instead, a specific number should be stated, "To increase sales of Purina brand cat food from $300 million to $345 million."
- *Time specific*: By what time should the objective be met? "To increase sales of Purina brand cat food between January 1, 2009 and December 31, 2010."
- *Compared to a benchmark*: If the objective is to increase sales by 15 percent, it is important to know the base line against which the objective will be measured. Will it be current sales? Last year's sales? For example, "To increase sales of Purina brand cat food by 15 percent over 2009 sales of $300 million."

Objectives must also be consistent with and indicate the priorities of the organization. Specifically, objectives flow from the business mission statement to the rest of the marketing plan. Exhibit 2.3 shows some well-stated and some

Exhibit 2.3

Examples of Marketing Objectives

Poorly Stated Objectives	Well-Stated Objectives
Our objective is to maximize profits.	Our objective is to achieve a 10 percent return on investment from January 1, 2009 until December 31, 2009, with a payback on new investments of no longer than December 31, 2013.
Our objective is to better serve customers.	Our objective is to obtain customer satisfaction ratings of 90 percent on the 2009 annual customer satisfaction survey, and to retain 85 percent of our 2009 customers as repeat purchasers in 2010.
Our objective is to be the best that we can be.	Our objective is to increase market share from 30 percent in 2009 to 40 percent in 2010 by increasing promotional expenditures by 14 percent over 2009 levels from January 1, 2010 to December 31, 2010.

REVIEW LEARNING OUTCOME

LO4 Describe the criteria for stating good marketing objectives

poorly stated objectives. Notice how well they do or do not meet the aforementioned criteria.

Carefully specified objectives serve several functions. First, they communicate marketing management philosophies and provide direction for lower-level marketing managers so that marketing efforts are integrated and pointed in a consistent direction. Objectives also serve as motivators by creating something for employees to strive for. When objectives are attainable and challenging, they motivate those charged with achieving the objectives. Additionally, the process of writing specific objectives forces executives to clarify their thinking. Finally, objectives form a basis for control; the effectiveness of a plan can be gauged in light of the stated objectives.

LO5

Competitive Advantage

Performing a SWOT analysis allows firms to identify their competitive advantage. A competitive advantage is a set of unique features of a company and its products that are perceived by the target market as significant and superior to the competition. It is the factor or factors that cause customers to patronize a firm and not the competition. There are three types of competitive advantages: cost, product/service differentiation, and niche strategies.

COST COMPETITIVE ADVANTAGE

Cost leadership can result from obtaining inexpensive raw materials, creating an efficient scale of plant operations, designing products for ease of manufacture, controlling overhead costs, and avoiding marginal customers. DuPont, for example, has an exceptional cost competitive advantage in the production of titanium dioxide. Technicians created a production process using low-cost feedstock, giving DuPont a 20 percent cost advantage over its competitors. The cheaper feedstock technology is complex and can be duplicated only by investing about $100 million and several years of testing time. Having a cost competitive advantage

competitive advantage
The set of unique features of a company and its products that are perceived by the target market as significant and superior to the competition.

cost competitive advantage
Being the low-cost competitor in an industry while maintaining satisfactory profit margins.

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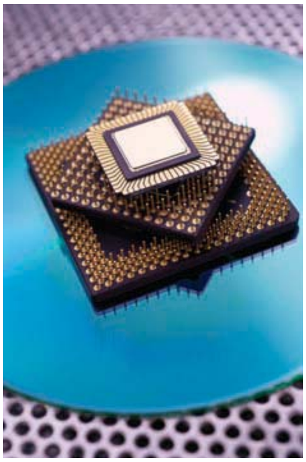
means being the low-cost competitor in an industry while maintaining satisfactory profit margins.

A cost competitive advantage enables a firm to deliver superior customer value. Wal-Mart, the world's leading low-cost general merchandise store, offers good value to customers because it focuses on providing a large selection of merchandise at low prices and good customer service. Wal-Mart is able to keep its prices down because it has strong buying power in its relationships with suppliers.

Costs can be reduced in a variety of ways.

- *Experience curves*: **Experience curves** tell us that costs decline at a predictable rate as experience with a product increases. The experience curve effect encompasses a broad range of manufacturing, marketing, and administrative costs. Experience curves reflect learning by doing, technological advances, and economies of scale. Firms like Boeing use historical experience curves as a basis for predicting and setting prices. Experience curves allow management to forecast costs and set prices based on anticipated costs as opposed to current costs.
- *Efficient labor*: Labor costs can be an important component of total costs in low-skill, labor-intensive industries such as product assembly and apparel manufacturing. Many U.S. manufacturers such as Nike, Levi Strauss, and Liz Claiborne have gone offshore to achieve cheaper manufacturing costs. Many American companies are also outsourcing activities such as data entry and other labor-intensive jobs.
- *No-frills goods and services*: Marketers can lower costs by removing frills and options from a product or service. Southwest Airlines, for example, offers low fares but no seat assignments or meals. Low costs give Southwest a higher load factor and greater economies of scale, which, in turn, mean lower prices for consumers.
- *Government subsidies*: Governments may provide grants and interest-free loans to target industries. Such government assistance enabled Japanese semiconductor manufacturers to become global leaders.
- *Product design*: Cutting-edge design technology can help offset high labor costs. BMW is a world leader in designing cars for ease of manufacture and assembly. Reverse engineering—the process of disassembling a product piece by piece to learn its components and obtain clues as to the manufacturing process—can also mean savings. Reverse engineering a low-cost competitor's product can save research and design costs. Japanese engineers have reverse engineered many products, such as computer chips coming out of Silicon Valley.
- *Reengineering*: Reengineering entails fundamental rethinking and redesign of business processes to achieve dramatic improvements in critical measures of performance. It often involves reorganizing from functional departments such as sales, engineering, and production to cross-disciplinary teams.
- *Production innovations*: Production innovations such as new technology and simplified production techniques help lower the average cost of production. Technologies such as computer-aided design and computer-aided manufacturing (CAD/CAM) and increasingly sophisticated robots help companies like Boeing, Ford, and General Electric reduce their manufacturing costs.
- *New methods of service delivery*: Medical expenses have been substantially lowered by the use of outpatient surgery and walk-in clinics. Airlines, such as Delta, are lowering reservation and ticketing costs by encouraging passengers to use the Internet to book flights and by providing self-check-in kiosks at the airport.



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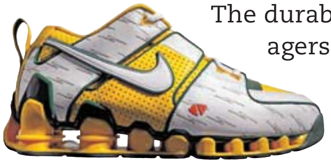
experience curves
Curves that show costs declining at a predictable rate as experience with a product increases.

PRODUCT/SERVICE DIFFERENTIATION COMPETITIVE ADVANTAGE



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Because cost competitive advantages are subject to continual erosion, product/service differentiation tends to provide a longer lasting competitive advantage. The durability of this strategy tends to make it more attractive to many top managers. A product/service differentiation competitive advantage exists when a firm provides something unique that is valuable to buyers beyond simply offering a low price. Examples include brand names (Lexus), a strong dealer network (Caterpillar Tractor for construction work), product reliability (Maytag appliances), image (Neiman Marcus in retailing), or service (FedEx). A great example of a company that has a strong product/service competitive advantage is Nike. Nike's advantage is built around one simple idea—product innovation. The company's goal is to think of something that nobody has thought of before or improve something that already exists. Nike Air, ACG, Nike Swift, and Nike Shox are examples of innovative shoes introduced by Nike.[4] Another example is PetSmart. Not only does PetSmart offer numerous products for all types of pets, it also offers services such as Pets-Hotel, grooming and training.[5]

product/service differentiation competitive advantage The provision of something that is unique and valuable to buyers beyond simply offering a lower price than the competition's.

niche competitive advantage The advantage achieved when a firm seeks to target and effectively serve a small segment of the market.

sustainable competitive advantage An advantage that can not be copied by the competition.

NICHE COMPETITIVE ADVANTAGE

A niche competitive advantage seeks to target and effectively serve a single segment of the market (see Chapter 8). For small companies with limited resources that potentially face giant competitors, niche targeting may be the only viable option. A market segment that has good growth potential but is not crucial to the success of major competitors is a good candidate for developing a niche strategy.

Many companies using a niche strategy serve only a limited geographic market. Buddy Freddy's is a very successful restaurant chain, but is found only in Florida. Migros is the dominant grocery chain in Switzerland. It has no stores outside that small country.

Block Drug Company uses niche targeting by focusing its product line on tooth products. It markets Polident to clean false teeth, Poligrip to hold false teeth, and Sensodyne toothpaste for persons with sensitive teeth. The Orvis Company manufactures and sells everything that anyone might ever need for fly fishing. Orvis is a very successful niche marketer.

BUILDING SUSTAINABLE COMPETITIVE ADVANTAGE

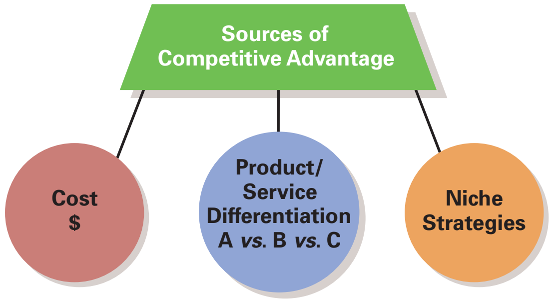
The key to having a competitive advantage is the ability to sustain that advantage. A sustainable competitive advantage is one that cannot be copied by the competition. Nike, discussed earlier, is a good example of a company that has a sustainable competitive advantage. Others include Rolex (high-quality watches), Nordstrom department stores (service), and Southwest Airlines (low price). In contrast, when Datril was introduced into the pain-reliever market, it was touted as being exactly like Tylenol, only cheaper. Tylenol responded by lowering its price, thus destroying Datril's competitive advantage and ability to remain on the market. In this case, low price was not a sustainable competitive advantage. Without a competitive advantage, target customers don't perceive any reason to patronize an organization instead of its competitors.

The notion of competitive advantage means that a successful firm will stake out a position unique in some manner from its rivals. Imitation of competitors indicates a lack of competitive advantage and almost ensures mediocre performance. Moreover, competitors rarely stand still, so it is not surprising that imitation causes managers to feel trapped in a seemingly endless game of catch-up. They are regularly surprised by the new accomplishments of their rivals.

REVIEW LEARNING OUTCOME

LO5 Identify sources of competitive advantage

To create sustainable competitive advantage, don't copy someone else, build your own:



Companies need to build their own competitive advantages rather than copy a competitor. The sources of tomorrow's competitive advantages are the skills and assets of the organization. Assets include patents, copyrights, locations, equipment, and technology that are superior to those of the competition. Skills are functions such as customer service that the firm performs better than its competitors. Netflix, for example, created and remains dominant in the market for renting movies by mail. Marketing managers should continually focus the firm's skills and assets on sustaining and creating competitive advantages.

Remember, a sustainable competitive advantage is a function of the speed with which competitors can imitate a leading company's strategy and plans. Imitation requires a competitor to identify the leader's competitive advantage, determine how it is achieved, and then learn how to duplicate it.

LO6 Strategic Directions

The end result of the SWOT analysis and identification of a competitive advantage is to evaluate the strategic direction of the firm. Selecting a strategic alternative is the next step in marketing planning.

STRATEGIC ALTERNATIVES

To discover a marketing opportunity, management must know how to identify the alternatives. One method for developing alternatives is Ansoff's strategic opportunity matrix (see Exhibit 2.4), which matches products with markets. Firms can explore these four options:

- *Market penetration*: A firm using the market penetration alternative would try to increase market share among existing customers. If Kraft Foods started a major campaign for Maxwell House coffee, with aggressive advertising and cents-off coupons to existing customers, it would be following a penetration strategy. McDonald's sold the most Happy Meals in history with a promotion that included Ty's Teeny Beanie Babies. Customer databases, discussed in Chapters 9 and 20, helped managers implement this strategy.
- *Market development*: Market development means attracting new customers to existing products. Ideally, new uses for old products stimulate additional sales among existing customers while also bringing in new buyers. McDonald's, for example, has opened restaurants in Russia, China, and Italy and is eagerly expanding into Eastern European countries. Sara Lee is entering the market for meals on the go by introducing Hillshire Farm Salad Entrees, kits that contain meat and other ingredients that the company already makes, to be added to lettuce.[6] In the nonprofit area, the growing emphasis on continuing education and executive development by colleges and universities is a market development strategy.
- *Product development*: A product development strategy entails the creation of new products for present markets. Several makers of men's suits have introduced new suits designed to be worn in hot weather. For example, Brooks Brothers has introduced a line of poplin suits with polyester fibers that move moisture away from the body. Joseph A. Bank Clothiers has created suits that

market penetration
A marketing strategy that tries to increase market share among existing customers.

market development
A marketing strategy that entails attracting new customers to existing products.

product development
A marketing strategy that entails the creation of new products for current customers.

Exhibit 2.4

Ansoff's Strategic Opportunity Matrix

	Present Product	New Product
Present Market	**Market penetration:** McDonald's sells more Happy Meals with Disney movie promotions.	**Product development:** McDonald's introduces premium salads and McWater.
New Market	**Market development:** McDonald's opens restaurants in China.	**Diversification:** McDonald's introduces line of children's clothing.

contain the same fibers NASA developed for spacesuits to prevent astronauts from getting overheated.[7]

Managers following the product development strategy can rely on their extensive knowledge of the target audience. They usually have a good feel for what customers like and dislike about current products and what existing needs are not being met. In addition, managers can rely on established distribution channels.

diversification
A strategy of increasing sales by introducing new products into new markets.

portfolio matrix
A tool for allocating resources among products or strategic business units on the basis of relative market share and market growth rate.

- Diversification: **Diversification** is a strategy of increasing sales by introducing new products into new markets. For example, Ralph Lauren developed a new brand of clothing called Rugby to appeal to young people from 14 to 29.[8] Sony practiced a diversification strategy when it acquired Columbia Pictures; although motion pictures are not a new product in the marketplace, they were a new product for Sony. Coca-Cola manufactures and markets water-treatment and water-conditioning equipment, which has been a very challenging task for the traditional soft drink company. A diversification strategy can be risky when a firm is entering unfamiliar markets. On the other hand, it can be very profitable when a firm is entering markets with little or no competition.

SELECTING A STRATEGIC ALTERNATIVE

Portfolio Matrix

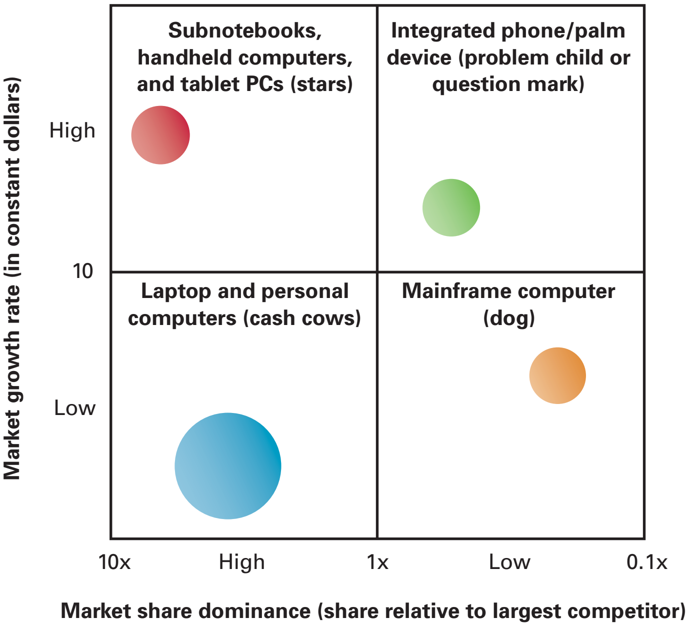
Recall that large organizations engaged in strategic planning may create strategic business units. Each SBU has its own rate of return on investment, growth potential, and associated risk. Management must find a balance among the SBUs that yields the overall organization's desired growth and profits with an acceptable level of risk. Some SBUs generate large amounts of cash, and others need cash to foster growth. The challenge is to balance the organization's "portfolio" of SBUs for the best long-term performance.

Companies often try to profit by expanding the lines of their most profitable brands (cash cows). Tide, for instance, has been expanded to include the Tide With Bleach Alternative featured in this advertisement.

To determine the future cash contributions and cash requirements expected for each SBU, managers can use the Boston Consulting Group's portfolio matrix. The **portfolio matrix** classifies each SBU by its present or forecast growth and market share. The underlying assumption is that market share and profitability are strongly linked. The measure of market share used in the portfolio approach is *relative market share,* the ratio between the company's share and the share of the largest competitor. For example, if firm A has a 50 percent share and the competitor has 5 percent, the ratio is 10 to 1. If firm A has a

Exhibit 2.5

Portfolio Matrix for a Large Computer Manufacturer



NOTE: The size of the circle represents the dollar sales relative to sales of other SBUs on the matrix—for example, 10x means sales are ten times greater than those of the next largest competitor.

10 percent market share and the largest competitor has 20 percent, the ratio is 0.5 to 1.

Exhibit 2.5 is a hypothetical portfolio matrix for a large computer manufacturer. The size of the circle in each cell of the matrix represents dollar sales of the SBU relative to dollar sales of the company's other SBUs. The following categories are used in the matrix:

- *Stars*: A **star** is a market leader and growing fast. For example, computer manufacturers have identified notebook and handheld models as stars. Star SBUs usually have large profits but need a lot of cash to finance rapid growth. The best marketing tactic is to protect existing market share by reinvesting earnings in product improvement, better distribution, more promotion, and production efficiency. Management must strive to capture most of the new users as they enter the market.
- *Cash cows*: A **cash cow** is an SBU that usually generates more cash than it needs to maintain its market share. It is in a low-growth market, but the product has a dominant market share. Personal computers and laptops are categorized as cash cows in Exhibit 2.5. The basic strategy for a cash cow is to maintain market dominance by being the price leader and making technological improvements in the product. Managers should resist pressure to extend the basic line unless they can dramatically increase demand. Instead, they should allocate excess cash to the product categories where growth prospects are the greatest. For instance, the Clorox Company owns Kingsford charcoal, the Glad brand of products, Fresh Step, Scoop Away and other pet litters, Black Flag pest control products, Brita water filtration systems, and K. C. Masterpiece barbecue sauce, among others. Traditionally, the company's cash cow has been Clorox bleach, which owns the lion's share of a low-growth market. The Clorox Company has been highly successful in stretching the Clorox line to include scented chlorine bleach as well as Clorox 2, chlorine-free bleach for colored clothing. Another example is Heinz, which has two cash cows: ketchup and Weight Watchers frozen dinners.
- *Problem children*: A **problem child,** also called a **question mark,** shows rapid growth but poor profit margins. It has a low market share in a high-growth industry. Problem children need a great deal of cash. Without cash support, they eventually become dogs. The strategy options are to invest heavily to gain better market share, acquire competitors to get the necessary market share, or drop the SBU. Sometimes a firm can reposition the products of the SBU to move them into the star category. Zima brand beer, targeted at Generation X, was a problem child for Adolph Coors Company. The company ultimately withdrew its heavy marketing investment in Zima and positioned it as a niche product.
- *Dogs*: A **dog** has low growth potential and a small market share. Most dogs eventually leave the marketplace. In the computer manufacturer example, the mainframe computer has become a dog. Other examples include Warner-Lambert's Reef mouthwash and Campbell's Red Kettle soups. Frito-Lay has produced several dogs, including Stuffers cheese-filled snacks, Rumbles granola nuggets, and Toppels cheese-topped crackers—a trio irreverently known as Stumbles, Tumbles, and Twofers. The strategy options for dogs are to harvest or divest.

star
In the portfolio matrix, a business unit that is a fast-growing market leader.

cash cow
In the portfolio matrix, a business unit that usually generates more cash than it needs to maintain its market share.

problem child (question mark)
In the portfolio matrix, a business unit that shows rapid growth but poor profit margins.

dog
In the portfolio matrix, a business unit that has low growth potential and a small market share.

After classifying the company's SBUs in the matrix, the next step is to allocate future resources for each. The four basic strategies are to:

- *Build*: If an organization has an SBU that it believes has the potential to be a star (probably a problem child at present), building would be an appropriate goal. The organization may decide to give up short-term profits and use its financial resources to achieve this goal. Procter & Gamble built Pringles from a money loser into a record profit maker.
- *Hold*: If an SBU is a very successful cash cow, a key goal would surely be to hold or preserve market share so that the organization can take advantage of the very positive cash flow. Bisquick has been a prosperous cash cow for General Mills for over two decades.
- *Harvest*: This strategy is appropriate for all SBUs except those classified as stars. The basic goal is to increase the short-term cash return without too much concern for the long-run impact. It is especially worthwhile when more cash is needed from a cash cow with long-run prospects that are unfavorable because of low market growth rate. For instance, Lever Brothers has been harvesting Lifebuoy soap for a number of years with little promotional backing.
- *Divest*: Getting rid of SBUs with low shares of low-growth markets is often appropriate. Problem children and dogs are most suitable for this strategy. Procter & Gamble dropped Cincaprin, a coated aspirin, because of its low growth potential.

REVIEW LEARNING OUTCOME

LO 6 Identify strategic alternatives

Market development = ↑ customers
Market penetration = ↑ share
Product development = ↑ products
Diversification = ↑ New Products + ↑ New Markets

LO 7
Describing the Target Market

marketing strategy
The activities of selecting and describing one or more target markets and developing and maintaining a marketing mix that will produce mutually satisfying exchanges with target markets.

market opportunity analysis (MOA)
The description and estimation of the size and sales potential of market segments that are of interest to the firm and the assessment of key competitors in these market segments.

Marketing strategy involves the activities of selecting and describing one or more target markets and developing and maintaining a marketing mix that will produce mutually satisfying exchanges with target markets.

TARGET MARKET STRATEGY

A market segment is a group of individuals or organizations that share one or more characteristics. They therefore may have relatively similar product needs. For example, parents of newborn babies need products such as formula, diapers, and special foods. The target market strategy identifies the market segment or segments on which to focus. This process begins with a **market opportunity analysis (MOA)**—the description and estimation of the size and sales potential of market segments that are of interest to the firm and the assessment of key competitors in these market segments. After the firm describes the market segments, it may target one or more of them. There are three general strategies for selecting target markets. Target market(s) can be selected by appealing to the entire market with one marketing mix, concentrating on one segment, or appealing to multiple market segments using multiple marketing mixes. The characteristics, advantages, and disadvantages of each strategic option are examined in Chapter 8. Target markets could be smokers who are concerned about white teeth (the target of Topol toothpaste), people concerned about sugar and calories in their soft drinks (Diet Pepsi), or college students needing inexpensive about-town transportation (Yamaha Razz scooter).

PR NEWSFOTO/©YOPLAIT KIDS

REVIEW LEARNING OUTCOME

LO7 Discuss target market strategies

Any market segment that is targeted must be fully described. Demographics, psychographics, and buyer behavior should be assessed. Buyer behavior is covered in Chapters 6 and 7. If segments are differentiated by ethnicity, multicultural aspects of the marketing mix should be examined. If the target market is international, it is especially important to describe differences in culture, economic and technological development, and political structure that may affect the marketing plan. Global marketing is covered in more detail in Chapter 5.

LO8 The Marketing Mix

marketing mix
A unique blend of product, place, promotion, and pricing strategies designed to produce mutually satisfying exchanges with a target market.

four Ps
Product, place, promotion, and price, which together make up the marketing mix.

The term **marketing mix** refers to a unique blend of product, place (distribution), promotion, and pricing strategies (often referred to as the **four Ps**) designed to produce mutually satisfying exchanges with a target market. The marketing manager can control each component of the marketing mix, but the strategies for all four components must be blended to achieve optimal results. Any marketing mix is only as good as its weakest component. For example, the first pump toothpastes were distributed over cosmetic counters and failed. Not until pump toothpastes were distributed the same way as tube toothpastes did the products succeed. The best promotion and the lowest price cannot save a poor product. Similarly, excellent products with poor placing, pricing, or promotion will likely fail.

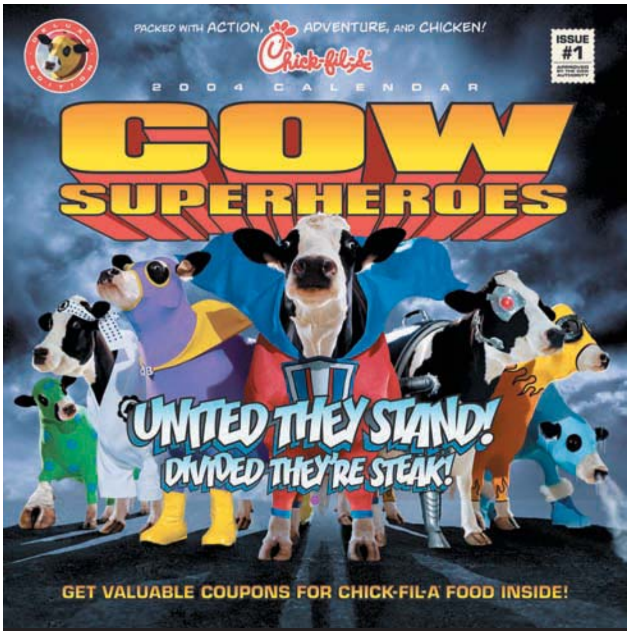
Successful marketing mixes have been carefully designed to satisfy target markets. At first glance, McDonald's and Wendy's may appear to have roughly identical marketing mixes because they are both in the fast-food hamburger business. However, McDonald's has been most successful at targeting parents with young children for lunchtime meals, whereas Wendy's targets the adult crowd for lunches and dinner. McDonald's has playgrounds, Ronald McDonald the clown, and children's Happy Meals. Wendy's has salad bars, carpeted restaurants, and no playgrounds.

Variations in marketing mixes do not occur by chance. Astute marketing managers devise marketing strategies to gain advantages over competitors and best serve the needs and wants of a particular target market segment. By manipulating elements of the marketing mix, marketing managers can fine-tune the customer offering and achieve competitive success.

PRODUCT STRATEGIES

Typically, the marketing mix starts with the product "P." The heart of the marketing mix, the starting point, is the product offering and product strategy. It is hard to design a place strategy, decide on a promotion campaign, or set a price without knowing the product to be marketed.

The product includes not only the physical unit but also its package, warranty, after-sale service, brand name, company image, value, and many other factors. A Godiva chocolate has many product elements: the chocolate itself, a fancy gold wrapper, a customer satisfaction guarantee, and the prestige of the Godiva brand name. We buy things not only for what they do (benefits) but also for what they mean to us (status, quality, or reputation).



PR NEWSFORO/©CHICK-FIL-A

The role of promotion is to inform, persuade, and remind. Chik-Fil-A's popular "Eat Mor Chikin" cows have been the subject of outdoor advertising, television advertising, and even a yearly calendar that contains over $20 worth of coupons for free food.

REVIEW LEARNING OUTCOME

LO8 Describe the elements of the marketing mix

Marketing Mix

Products can be tangible goods such as computers, ideas like those offered by a consultant, or services such as medical care. Products should also offer customer value. Product decisions are covered in Chapters 10 and 11, and services marketing is detailed in Chapter 12.

PLACE (DISTRIBUTION) STRATEGIES

Place, or distribution, strategies are concerned with making products available when and where customers want them. Would you rather buy a kiwi fruit at the 24-hour grocery store within walking distance or fly to Australia to pick your own? A part of this place "P" is physical distribution, which involves all the business activities concerned with storing and transporting raw materials or finished products. The goal is to make sure products arrive in usable condition at designated places when needed. Place strategies are covered in Chapters 15 and 16.

PROMOTION STRATEGIES

Promotion includes advertising, public relations, sales promotion, and personal selling. Promotion's role in the marketing mix is to bring about mutually satisfying exchanges with target markets by informing, educating, persuading, and reminding them of the benefits of an organization or a product. A good promotion strategy, like using the Dilbert character in a national promotion strategy for Office Depot, can dramatically increase sales. Good promotion strategies do not guarantee success, however. Despite massive promotional campaigns, the movies *The Alamo* and *The Ladykillers* had disappointing box-office returns. Each element of the promotion "P" is coordinated and managed with the others to create a promotional blend or mix. These integrated marketing communications activities are described in Chapters 16, 17, and 18. Technology-driven aspects of promotional marketing are covered in Chapter 21.

PRICING STRATEGIES

Price is what a buyer must give up to obtain a product. It is often the most flexible of the four marketing mix elements—the quickest element to change. Marketers can raise or lower prices more frequently and easily than they can change other marketing mix variables. Price is an important competitive weapon and is very important to the organization because price multiplied by the number of units sold equals total revenue for the firm. Pricing decisions are covered in Chapters 19 and 20.

LO9 Following Up on the Marketing Plan

implementation
The process that turns a marketing plan into action assignments and ensures that these assignments are executed in a way that accomplishes the plan's objectives.

IMPLEMENTATION

Implementation is the process that turns a marketing plan into action assignments and ensures that these assignments are executed in a way that accomplishes the plan's objectives. Implementation activities may involve detailed job assignments, activity descriptions, timelines, budgets, and lots of communication. Although implementation is essentially "doing what you said you were going to do," many organizations repeatedly experience failures in strategy implementation. Brilliant marketing plans are doomed to fail if they are not properly implemented. These detailed communications may or may not be part of the written marketing plan. If they are not part of the plan, they should be specified elsewhere as soon as the plan has been communicated.

EVALUATION AND CONTROL

evaluation
Gauging the extent to which the marketing objectives have been achieved during the specified time period.

control
Provides the mechanisms for evaluating marketing results in light of the plan's objectives and for correcting actions that do not help the organization reach those objectives within budget guidelines.

marketing audit
A thorough, systematic, periodic evaluation of the objectives, strategies, structure, and performance of the marketing organization.

After a marketing plan is implemented, it should be evaluated. Evaluation entails gauging the extent to which marketing objectives have been achieved during the specified time period. Four common reasons for failing to achieve a marketing objective are unrealistic marketing objectives, inappropriate marketing strategies in the plan, poor implementation, and changes in the environment after the objective was specified and the strategy was implemented.

Once a plan is chosen and implemented, its effectiveness must be monitored. Control provides the mechanisms for evaluating marketing results in light of the plan's objectives and for correcting actions that do not help the organization reach those objectives within budget guidelines. Firms need to establish formal and informal control programs to make the entire operation more efficient.

Perhaps the broadest control device available to marketing managers is the marketing audit—a thorough, systematic, periodic evaluation of the objectives, strategies, structure, and performance of the marketing organization. A marketing

ETHICS in Marketing

Word Games[9]

Company-sponsored word of mouth promotions, or "buzz marketing," are the newest way for companies to grab attention for their products. Buzz marketing is thought to be particularly effective with teens because they watch less TV, and are cynical about the many marketing messages that bombard them daily. This technique is designed to get teens talking about products in their ordinary, everyday conversations.

Buzz marketing campaigns can be very effective. For example, the Rock Bottom brew pub chain reported a 76 percent increase in yearly revenues after BzzAgent, Boston launched a 13-week, word-of-mouth campaign using over 1000 of its "agents" to talk about the pub. UPN, the network that airs the series "America's Next Top Model," solicited the help of Alloy.com, a shopping and lifestyle Web site aimed at teen girls, to find 500 "insiders" who could generate buzz about the show, which needed a ratings boost. Alloy chose girls who were deemed to be popular, provided them with party kits, and urged them to invite an average of 4 friends to their homes to watch "Top Model." The ratings increased among the teen segment. Proctor and Gamble has an in-house buzz team called "Tremor."

According to estimates published by JWT Worldwide in New York, over 85 percent of the country's top 1000 marketing firms use some from of word of mouth tactics. The growth of this industry is also reflected in the asking prices of teen social networking sites like MySpace, Sconex (a high school oriented site) and Facebook. These sites replace the past model for Web pages in which a publisher posted user-generated content. Social networking sites are seen by marketers as a cutting edge opportunity to get kids excited about a product by having them talk about it on their own.

While the buzz marketing industry is growing, watchdog groups have challenged the ethics of the technique directed at teens. A word-of-mouth campaign begins when a buzz marketing firm recruits a group of kids called "connectors" to get the talk going. Some companies claim to just expose kids to new products and hope they like them enough to tell their friends. However, it is common for the partner kids to receive free samples of the product or other incentives. Other issues include whether parents are approached before kids become involved in buzz marketing campaigns, and whether kids disclose to their friends that they have a relationship with the marketer. The Portland, Oregon advocacy group Commercial Alert sent a letter to the Federal Trade Commission to ask them to investigate Tremor for its activities. Their position is that teens are more impressionable than adults and so are easy to deceive.

Is it right for companies to use teens as buzz agents for their products? Should participating teens be required to tell their friends that they have a relationship with the marketer? Should parents have to give permission for their kids to be a buzz agent?

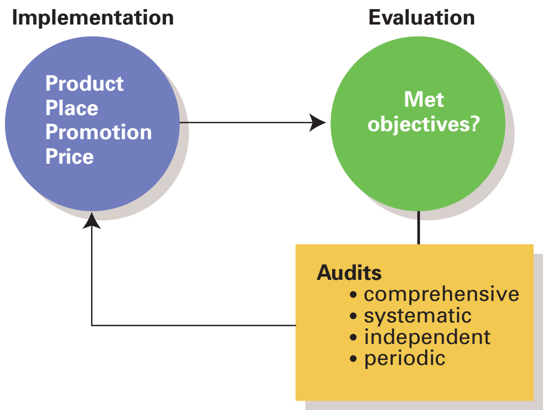
audit helps management allocate marketing resources efficiently. It has four characteristics:

- *Comprehensive*: The marketing audit covers all the major marketing issues facing an organization and not just trouble spots.
- *Systematic*: The marketing audit takes place in an orderly sequence and covers the organization's marketing environment, internal marketing system, and specific marketing activities. The diagnosis is followed by an action plan with both short-run and long-run proposals for improving overall marketing effectiveness.
- *Independent*: The marketing audit is normally conducted by an inside or outside party who is independent enough to have top management's confidence and to be objective.
- *Periodic*: The marketing audit should be carried out on a regular schedule instead of only in a crisis. Whether it seems successful or is in deep trouble, any organization can benefit greatly from such an audit.

Although the main purpose of the marketing audit is to develop a full profile of the organization's marketing effort and to provide a basis for developing and revising the marketing plan, it is also an excellent way to improve communication and raise the level of marketing consciousness within the organization. It is a useful vehicle for selling the philosophy and techniques of strategic marketing to other members of the organization.

REVIEW LEARNING OUTCOME

LO 9 Explain why implementation, evaluation, and control of the marketing plan are necessary



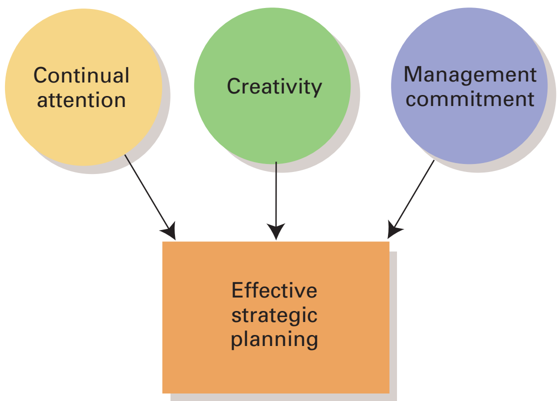
LO 10
Effective Strategic Planning

Effective strategic planning requires continual attention, creativity, and management commitment. Strategic planning should not be an annual exercise, in which managers go through the motions and forget about strategic planning until the next year. It should be an ongoing process because the environment is continually changing and the firm's resources and capabilities are continually evolving.

Sound strategic planning is based on creativity. Managers should challenge assumptions about the firm and the environment and establish new strategies. For example, major oil companies developed the concept of the gasoline service station in an age when cars needed frequent and rather elaborate servicing. They held on to the full-service approach, but independents were quick to respond to new realities and moved to lower-cost self-service and convenience-store operations. The majors took several decades to catch up.

REVIEW LEARNING OUTCOME

LO 10 Identify several techniques that help make strategic planning effective



Perhaps the most critical element in successful strategic planning is top management's support and participation. For example, Michael Anthony, CEO of Brookstone, Inc., and the Brookstone buying team earn hundreds of thousands of frequent flyer miles searching the world for manufacturers and inventors of unique products that can be carried in its retail stores, catalogs, and Internet site. Anthony has co-developed some of these products and has also been active in remodeling efforts for Brookstone's 250 permanent and seasonal stores.

3 < Types of competitive advantages

4 < Elements of the marketing mix; quadrants in the BCG matrix

Macroenvironmental forces affecting marketing > **6**

40 < Size of the market commanded by 9- to 13-year-old girls

Debut of the BCG portfolio matrix > **1996**

Review and Applications

LO 1

Understand the importance of strategic marketing and know a basic outline for a marketing plan. Strategic marketing planning is the basis for all marketing strategies and decisions. The marketing plan is a written document that acts as a guidebook of marketing activities for the marketing manager. A marketing plan provides the basis by which actual and expected performance can be compared. Although there is no set formula or a single correct outline, a marketing plan should include basic elements such as stating the business mission, setting objectives, performing a situation analysis of internal and external environmental forces, selecting target market(s), delineating a marketing mix (product, place, promotion, and price), and establishing ways to implement, evaluate, and control the plan.

1.1 Your cousin wants to start his own business, but he has decided not to write a marketing plan because he thinks that preparing one would take too long. He says he doesn't need a formal proposal because he has already received funding from your uncle. Explain why it is important for him to write a plan anyway.

WRITING

1.2 After graduation, you decide to take a position as the marketing manager for a small snack-food manufacturer. The company, Shur Snak, is growing, and this is the first time that the company has ever employed a marketing manager. Consequently, there is no marketing plan in place for you to follow. Outline a basic marketing plan for your boss to give her an idea of the direction you want to take the company.

ONLINE

1.3 How are Coke and Pepsi using their Web sites, http://www.coke.com and http://www.pepsi.com, to promote their newest product offerings? Do you see hints of any future strategies the companies might implement? Where?

LO 2

Develop an appropriate business mission statement. The mission statement is based on a careful analysis of benefits sought by present and potential customers and an analysis of existing and anticipated environmental conditions. The firm's mission statement establishes boundaries for all subsequent decisions, objectives, and strategies. A mission statement should focus on the market or markets the organization is attempting to serve rather than on the good or service offered.

ONLINE

2.1 Thinking back to question 1.2, write a business mission statement for Shur Snak. What elements should you include? Evaluate the mission statement you wrote against some of those you found online in question 2.1.

LO 3

Explain the components of a situation analysis. In the situation (or SWOT) analysis, the firm should identify its internal strengths (S) and weaknesses (W) and also examine external opportunities (O) and threats (T). When examining external opportunities and threats, marketing managers must analyze aspects of the marketing environment in a process called environmental scanning. The six most often studied macroenvironmental forces are social, demographic, economic, technological, political and legal, and competitive.

ONLINE

3.1 Competition in the private courier sector is fierce. UPS and FedEx dominate, but other companies, such as DHL and even the United States Postal Service (USPS), still have a decent chunk of the express package delivery market. Perform a mini-situation analysis on one of the companies listed below by stating one strength, one weakness, one opportunity, and one threat. You may want to consult the following Web sites as you build your grid:

UPS	http://www.ups.com	DHL	http:/www.dhl-usa.com
FedEx	http://www.fedex.com	USPS	http://www.usps.gov

LO4

Describe the criteria for stating good marketing objectives. Objectives should be realistic, measurable, and time specific. Objectives must also be consistent and indicate the priorities of the organization.

4.1 Building on the Shur Snak example, imagine that your boss has stated that the marketing objective of the company is to do the best job of satisfying the needs and wants of the customer. Explain that although this objective is admirable, it does not meet the criteria for good objectives. What are these criteria? What is a specific example of a better objective for Shur Snak?

LO5

Identify sources of competitive advantage. A competitive advantage is a set of unique features of a company and its products that are perceived by the target market as significant and superior to the competition. There are three types of competitive advantages: cost, product/service differentiation, and niche strategies. Sources of cost competitive advantages include experience curves, efficient labor, no-frills goods and services, government subsidies, product design, reengineering, product innovations, and new methods of service delivery. A product/service differentiation competitive advantage exists when a firm provides something unique that is valuable to buyers beyond just low price. Niche competitive advantages come from targeting unique segments with specific needs and wants. The goal of all these sources of competitive advantage is to be sustainable.

TEAM

5.1 Break into small groups and discuss examples (at least two per person) of the last few products you have purchased. What specific strategies were used to achieve competitive advantage? Is that competitive advantage sustainable against the competitors?

LO6

Identify strategic alternatives. The strategic opportunity matrix can be used to help management develop strategic alternatives. The four options are market penetration, product development, market development, and diversification. In selecting a strategic alternative, managers may use a portfolio matrix, which classifies strategic business units as stars, cash cows, problem children, or dogs, depending on their present or projected growth and market share.

6.1 Based on your SWOT analysis, decide what the strategic growth options are for the company you chose in question 3.1.

LO7

Discuss target market strategies. The target market strategy identifies which market segment or segments to focus on. This process begins with a market opportunity analysis (MOA), which describes and estimates the size and sales potential of market segments that are of interest to the firm. In addition, an assessment of key competitors in these market segments is performed. After the market segments are described, one or more may be targeted by the firm. The three strategies for selecting target markets are appealing to the entire market with one marketing mix, concentrating on one segment, or appealing to multiple market segments using multiple marketing mixes.

7.1 You are given the task of deciding the marketing strategy for a transportation company. How do the marketing mix elements change when the target market is (a) low-income workers without personal transportation, (b) corporate international business travelers, or (c) companies with urgent documents or perishable materials to be delivered to customers?

LO 8

Describe the elements of the marketing mix. The marketing mix (or four Ps) is a blend of product, place, promotion, and pricing strategies designed to produce mutually satisfying exchanges with a target market. The starting point of the marketing mix is the product offering. Products can be tangible goods, ideas, or services. Place (distribution) strategies are concerned with making products available when and where customers want them. Promotion includes advertising, public relations, sales promotion, and personal selling. Price is what a buyer must give up to obtain a product and is often the easiest to change of the four marketing mix elements.

TEAM

8.1 Choose three or four other students and make up a team. Create a marketing plan to increase enrollment in your school. Describe the four marketing mix elements that make up the plan.

LO 9

Explain why implementation, evaluation, and control of the marketing plan are necessary. Before a marketing plan can work, it must be implemented; that is, people must perform the actions in the plan. The plan should also be evaluated to see if it has achieved its objectives. Poor implementation can be a major factor in a plan's failure. Control provides the mechanisms for evaluating marketing results in light of the plan's objectives and for correcting actions that do not help the organization reach those objectives within budget guidelines.

TEAM

9.1 Have your school enrollment marketing plan team (from question 8.1) develop a plan to implement, evaluate, and control the marketing strategy.

LO 10

Identify several techniques that help make strategic planning effective. First, management must realize that strategic planning is an ongoing process and not a once-a-year exercise. Second, good strategic planning involves a high level of creativity. The last requirement is top management's support and cooperation.

10.1 What techniques can make your school enrollment marketing plan more effective?

Key Terms

Exercises

APPLICATION EXERCISE

As you now know from reading the chapter, an important part of the strategy-making process involves scanning the environment for changes that affect your marketing efforts. This exercise is designed to introduce you to the business press and to help you make the connection between the concepts you learn in the classroom and real-world marketing activities.

Activities

1. Find a current article of substance in the business press (*The Wall Street Journal*, *The Financial Times*, *Fortune*, *BusinessWeek*, *Inc.*, etc.) that discusses topics you have covered in this

course. Although this is only Chapter 2, you will be surprised by the amount of terminology you have already learned. If you are having trouble finding an article, read through the table of contents at the beginning of the book to familiarize yourself with the names of concepts that will be presented later in the course. Read your article carefully, making notes about relevant content.

2. Write a one-paragraph summary of the key points in your article; then write a list of the terms or concepts critical to understanding the article. Provide definitions of those terms. If you are unfamiliar with a term or concept that is central to the article, do some research in your textbook or see your professor during office hours. Relate these key points to the concepts in your text by citing page numbers.
3. Explain the environments that are relevant to the situation presented in the article. (Chapter 4 contains a full list of environmental factors.)

ETHICS EXERCISE

Abercrombie & Fitch, a retail clothing chain based in New Albany, Ohio, launched a line of thong underwear for preteen girls. Words like "eye candy" and "wink wink" were printed on the front of the skimpy underwear that some argued would fit girls aged 5 to 10. Abercrombie is known for its provocative ads and sexually oriented catalogs. Supporters of the strategy claim that producing thong-style underwear for 10- to 16-year olds is a good move; critics think that the line is tasteless and that marketing it to young girls is contemptuous.

Questions

1. Is marketing adult-styled undergarments to a younger audience unethical? Why or why not?
2. Would Abercrombie have been in the spotlight had the sexy words been omitted from the product? Explain your answer.

PR NEWSFOTO/©PALM SPRINGS PAVILLION THEATER

Case Study: Cirque Du Soleil

THE FIRE WITHIN

A 27-foot-long bronze clown shoe is the only indication that there is something otherworldly within the concrete walls of the large, rather nondescript building. Located in Montreal, the building is home to what many feel is the most successful entertainment company in the world—Cirque du Soleil.

The company's massive headquarters houses practice rooms the size of airplane hangars where cast members work on their routines. More than 300 seamstresses, engineers, and makeup artists sew, design, and build custom materials for exotic shows with stage lives of 10 to 12 years. In fact, the production staff often invents materials, such as the special waterproof makeup required for the production of *O*, a show performed mostly in a 1.5 million-gallon pool of water that was also specially designed and engineered by Cirque employees. Another key in-house resource is Cirque's team of 32 talent scouts and casting staff that recruits and cultivates performers from all over the world. The department maintains a database of 20,000 names, any of whom could be called at any time to join the members of Cirque's cast, who number 3,500 and come from over 40 countries.

Shows with exotic names like *Mystère, La Nouba, O, Dralion, Varekai*, and *Zumanity* communicate through style and tone that they are intended to do more than just amuse. Cirque designs productions with distinct personalities that are meant to evoke awe, wonder, inspiration, and reflection. As one cast member put it, "The goal of a Cirque performer is not just to perform a quadruple somersault, but to treat it as some manifestation of a spiritual, inner life. Like in dance, the goal is . . . to have a language, a conversation, with the audience."

Incredibly, every one of the 15 shows that Cirque has produced over its 20-year history has returned a profit. In contrast, 90 percent of the high-budget Broadway shows that strive to reach the same target market fail to break even. Cirque's statistics, however, are eye-popping. *Mystère*, which opened at the Treasure Island hotel and casino in Las Vegas in 1993 and still runs today, cost $45 million to produce and has returned over $430 million; *O*, which opened at the Bellagio hotel and casino in 1998, cost $92 million to produce and has already returned over $480 million. Though the company splits about half of its profits with its hotel and casino partners, those same partners sometimes absorb up to 75 percent of Cirque's production costs.

At the helm of this incredible business machine is the dynamic duo of Franco Dragone and Daniel Lamarre. Dragone, a Belgian, is the creative force behind most of the company's ten current productions, and Lamarre, a former television executive, presides over show and new venture development. Together, they have transformed a one-tour, one-residence circus company into an entertainment powerhouse with five simultaneous world tours; four permanent facilities in Las Vegas—Treasure Island, the Bellagio, New York–New York, and the MGM Grand—all of which are part of the Mirage family of casinos; another permanent theater at Disney World; and a series of shows on the cable television channel Bravo that has already won an Emmy.

Lamarre claims that his business is successful because he and his staff "let the creative people run it." He guides the company with an invisible hand, making sure that business policies do not interfere with the creative process; it is Dragone and his team of creative and production personnel, not a predetermined budget, that defines the content, style, and material requirements for each project. Because of their sound planning, Cirque du Soleil can claim that it is one of the world's elite businesses, as well as one of the world's elite entertainment companies.[10]

Questions

1. Based on what you have read in the case, outline a rudimentary SWOT analysis for Cirque du Soleil.
2. List and describe at least three keys to Cirque du Soleil's competitive advantage.
3. Explain how Cirque du Soleil implements, evaluates, and controls the elements of its marketing plan.

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Company Clips

METHOD – HEALTHY HOME

Cash-strapped startup companies generally do not spend a great deal of time and money on planning. Founders are so busy with the rudiments of business—finding customers and creating, manufacturing, and delivering the product—that they may even forget important things, like invoicing. Eric Ryan and Adam Lowry reinforce this notion in the opening of the second method video segment. Nonetheless, strategic planning is an important part of successful marketing. Listen closely to the segment, which introduces method's CEO, Alastair Dorward, and gauge for yourself how much planning you think this innovative startup did before launching its brand.

Questions

1. Based on what you heard in the video, does method have a marketing plan?
2. Explain the elements that make up method's competitive advantage. Is it sustainable?
3. What are the elements in method's marketing mix?
4. What are method's target market strategies and how does it use them in its operations?

Marketing & You Results

The higher your score, the greater importance you place on planning. You also develop plans more often and devote more energy to the planning process. High scores also indicate a motivation to work "smart" and efficiently. If your score was low, you are less inclined to spend energy planning and, as a result, may have lower performance.

© TODD ROSENBERG/KELLOGG COMPANY/PRNEWSFOTO/ AP TOPIC GALLERY.

Marketing Plan Appendix

A

I. Company Description

II. Business Mission

III. Situation Analysis

- Industry Analysis
- SWOT Analysis

IV. Marketing Objective

V. Marketing Strategy

- Target Marketing Strategy
- Marketing Mix
    - Product
    - Place/Distribution
    - Promotion
    - Price

VI. Implementation, Evaluation, and Control

- Marketing Research
- Organizational Structure and Plan
- Financial Projections
- Implementation Timetable
- Summary

e-motionsoftware
we keep the business of business moving

I COMPANY DESCRIPTION

Scott Keohane and a partner founded e-motion software in 2003 and established its worldwide headquarters in Austin, Texas. They envisioned software solutions that conformed to a particular business, not the other way around, with products designed to (1) improve operating efficiency, (2) empower users, (3) enhance security, (4) improve ROI, and (5) streamline business processes. [Ch. 1: Market Orientation—focusing upon customer needs and integrating all activities to readily provide customer satisfaction, while achieving long-term company goals.] Ultimately, however, Keohane's partner did not want to remain with the company. Keohane converted the partner's shares into a note, according to the partnership agreement the two had in place.

The origins of the company were based in Keohane's 10 years of entrepreneurial endeavors, with four years of this time spent as an independent consultant in the Oracle applications marketplace. Oracle is the world's largest enterprise software company. According to Oracle's Web site, the company's business is information—how to manage it, use it, share it, and protect it. Commercial enterprise information management software systems, such as those offered by Oracle, promised seamless integration of all information flowing through a company.

In a global marketplace in which external company collaborations are driving business efforts and internal cross-functional integration is critical for timely decision making, enterprise systems could help position companies in a highly competitive environment. [Ch. 7: Business Marketing—e-motion software operates as a business marketer since it provides goods and services to organizations for purposes other than personal consumption.] Enterprise systems, such as the Oracle E-Business Suite, provided a simplified, unifying corporate technology platform. This type of platform enabled companies to utilize high-quality internal and external information both strategically and tactically. There were numerous product families in the E-Business Suite (e.g., advanced procurement, contracts, performance management, customer data/relationship management, financial, human resource management, logistics, manufacturing, marketing, order management, projects, sales, service, and supply chain management). [Ch. 10: E-Business is one product line in Oracle's product mix width. There are numerous product items in this product line.]

As an independent consultant, Keohane was continually asked to customize existing Oracle technology or create one-off applications to meet common requirements. The need for third-party products that would withstand upgrades to the underlying Oracle architecture was identified and e-motion software was formed. The overall business concept was to utilize the Oracle E-Business Suite as the underlying framework for customization to fit a particular customer's needs. Soon after incorporation, e-motion software became a member of the Oracle Partner Network. By joining the Oracle Partner Network, e-motion software gained access to Oracle Software Licenses, technical training, marketing funds, and co-marketing opportunities. [Ch. 6: Strategic Partnership—e-motion software partnered with Oracle so as to improve the offerings to its customers.]

II BUSINESS MISSION

[Ch. 2: The foundation of any marketing plan is the firm's mission statement.]
E-motion software is committed to the Oracle E-Business Suite of Applications and will provide a level of support that is unmatched in the industry. The company's goals are to make Oracle Applications more reliable, to enhance the Applications' functionality, and to make the Suite's use more efficient. [Ch. 2: What business is e-motion software in?] The company's products offer an attractive alternative to in-house development and support. E-motion software customers will be utilizing functional products that are self-funding. That is, the savings achieved through a more efficient workforce and security enhances will far exceed the cost of the company's products. The company's commitment extends from the methods used to build e-motion software products to the company's simple installation procedures to the post-installation service. E-motion software products run on multiple server platforms, require no customization, and are fully compatible with existing hardware and software warranties. [Ch. 2: E-motion software is focused on markets served and benefits sought by its customers.]

III SITUATION ANALYSIS

[Ch. 2: Marketers must understand the current and potential environment before defining marketing tactics.]

Industry Analysis

[Ch. 2: Environmental scanning is the collection and interpretation of information about forces, events, and relationships in the external environment that may affect the future of the organization or the implementation of the marketing plan.]

Trends The Enterprise Resource Planning (ERP) community has undergone a radical change since the turn of the century. Historically, applications were designed for the professional user or technology expert. Today's marketplace, however, has shifted from the professional user to employee users. That is, employees in all functional areas have access to and utilize information from the ERP application. Thus, ERP providers have shifted to developing applications intended for individual employee use instead of releasing bigger applications designed for the professional user. These self-service, employee based applications have fundamentally changed the way ERP applications are sold, implemented, and administered. Professional users are no longer the keepers of the data, manually entering and updating data from forms and memos. They have now become administrators in charge of ensuring data integrity. The promise of turning departments, such as HR and benefits, from manual intensive data entry shops to proactive reporting shops has shifted the marketplace to self-service suite applications. This emerging trend has prompted the development of self-service applications that enable employees to utilize systems within their individual realms of expertise, yet systems that are integrated across the firm.

Competitors E-motion software represents a new voice within the Oracle community. The company is creating a new niche in the marketplace and, as such, competition comes from a variety of sources. There are currently no head-to-head competitors. Competition can be split into three very distinct groups: Oracle, consulting firms, and in-house development centers.

Oracle Apart from being the company that created the ERP industry, Oracle has resources that dwarf every other company in the ERP marketplace. The availability of capital and the size of the development group infer that Oracle can simply reallocate a small development team to work on competing products. Oracle has, however, repeatedly released products that were little more than advanced betas, resulting in weeks of downtime for companies implementing the new products. By building applications that require no customization to Oracle code, e-motion software can confidently assure its customers that its products will work.

Consulting firms could advise the client to include the cost of custom application development into the total cost of the consulting engagement. This is standard protocol for competing consultancies and would effectively stop e-motion software from entering into a client site. Most consultancies, however, do not have a support and development center to handle ongoing system management. E-motion software will compete directly with consultancies by providing superior service at an affordable price.

The *In-house development centers (IHDCs)* poses a tricky problem for e-motion software. If a company has an IHDC, it is usually a trusted source that knows the company, its standards, and its software.

Additionally, the IHDC is usually considered a "no-cost" center since salaries are already included in the company's budget. Thus, program development and implementation is considered just another project with no additional cost. On the positive side, information technology (IT) budgets were slashed and IT departments scaled down over the past few years. While IT spending has begun to trend upward again, the creation of IHDC units has lagged this spending trend. E-motion software plans to capitalize on this lag in IHDC unit development and upward spending trend.

Customer Profile The marketplace has moved from professional users to employee users. Basically, professional users are now babysitters, ensuring that employees do not enter incorrect information into the system. This poses quite a quandary. Professional users must maintain the integrity of the system, while releasing control of it at the same time. This often forces the professional user to become a reactive unit, rushing to fix things when they breakdown. Employee users do not generally know the idiosyncrasies of the ERP system, of which there are many. Thus to maintain system integrity and ensure data reliability, professional users are often double-checking employee's data entry and also answering help desk calls regarding how to use the system. This is not, however, what a self-service ERP solution is designed to deliver. E-motion software proposes to enter the self-service arena with a broad range of products designed to regain the efficiencies promised by self-service applications.

Technology The costs of developing and maintaining an ERP solution require that the underlying technology be relevant for several years after product purchase and installation. The rapid emergence of Internet-based transactions (e.g., banking, loan applications, etc.) brought self-service applications to the forefront of business opportunity. Initially, Oracle attempted to use a mix of PL/SQL and DHTML code in the self-service offerings. This mix, however, did not provide the best looking applications, had little functionality, and were difficult to implement. Oracle then switched to using Java Server Pages (JSP) as its self-service foundation, with PL/SQL and HTML as the accessory languages. Products with the JSP foundation were well received in the marketplace. e-motion software plans to adhere to Oracle's decision to use JSP, especially since JSP offers e-motion software some key benefits: (1) JSP is robust and flexible allowing all applications to use the same coding techniques, (2) JSP is recyclable which means that e-motions software can leverage existing code across new applications, (3) JSP is accessible since Java is one of the most well known programming languages, (4) JSP is portable, allowing e-motion software to easily enter other ERP markets, and (5) the use of JSP means that e-motion software will always comply with Oracle approved practices.

SWOT Analysis

The strengths, weaknesses, opportunities, and threats (SWOT) analysis provides a snapshot of e-motion software's internal strengths and weaknesses and external opportunities and threats. [Ch. 2: Performing a SWOT analysis allows firms to identify their competitive advantage.]

Strengths

[Ch.2: Strengths are *internal* to the firm.]

- Founder—Scott Keohane is extremely knowledgeable about the third-party marketplace, and he is also personally and financially dedicated to making the business a success.
- Active and committed advisory council.
- Reliable products and product support.
- Member of Oracle Partner Network.

Weaknesses

[Ch.2: Weaknesses are *internal* to the firm.]

- A one-person company that has to supplement the company with independent consulting services.
- Not enough time dedicated to company development.
- Though it has considerable anecdotal information, the company is lacking in marketing research.
- Financial resources.

Opportunities

[Ch.2: Opportunities are *external* to the firm.]

- Changing marketplace that coincides with e-motion software's product development.
- The move toward employee users instead of professional users.
- Growth market.
- Technological changes.
- Refocus on IT applications.
- Persistent threat of security breaches.
- Growing focus on cross-functional interactions in the business press.
- New entries into the workforce (e.g., recent college graduates) are trained to use computers in decision making and thus expect companies to have data programs in place.

Threats

[Ch.2: Threats are *external* to the firm.]

- Competitors—all three groups of competitors are likely to have deeper pockets than e-motion software.
- Offerings can be duplicated by knowledgeable experts.

- Limited market access across the United States.
- Economies of scale in larger companies such as Oracle.
- IT departments do not have unlimited budgets.

IV MARKETING OBJECTIVE

The marketing objective is to establish the company as an expert in the third-party marketplace. [Ch. 2: The marketing objective statement provides a look at what the company seeks to accomplish. It is consistent with the priorities of the organization.] The third party product market for functions that are specifically designed for integration with Oracle Applications is in its infancy. E-motion software has to establish itself as a leader in this new marketplace. To accomplish this objective, customers must see that e-motion software products are safe and secure and that they do not affect existing Oracle functionality or their Oracle warranty.

Objective Metric: Three major Oracle clients by the end of 2005 [Ch. 2: Stated objectives must be measurable and time specific.]

To accomplish this marketing objective, e-motion software must obtain three major Oracle clients by the end of 2005. These clients will serve as reference sites for the company. These clients will enable e-motion software to demonstrate the gains achieved by using e-motion software products. As such, the clients need to be vocal and create viral marketing within the industry.

Objective Metric: One client in each region of the United States by the end of 2006 [Ch. 2: Stated objectives must be measurable and time specific.]

Given the close-knit nature of Oracle clients through organizations such as the Oracle Application User's Group (OAUG), e-motion software needs to gain clients within each of the major geographic areas in the United States: Northeast, Mid-Atlantic, Southeast, Midwest, Northwest, and West Coast.

V MARKETING STRATEGY

Target Market Strategy

E-motion software's sales plan is based on the company's understanding of the marketplace and on how it will resolve inefficiencies with the use of the Oracle E-Business Suite of Applications. From his consulting experience in helping potential clients install and maintain their individualized suite of applications, Keohane has considerable understanding of users' needs. To obtain clients, e-motion software will rely on continuing existing relationships with prospective clients, maintaining ongoing relationships with other consulting firms, and reaching new clients via marketing and sales initiatives.

Geographically, e-motion software will direct its marketing and sales efforts within the contiguous United States. [Ch. 8: Geographic segmentation refers to segmenting markets by region of a country or the world, market size, market density, or climate.] Though global operations are potential clients, the current size of e-motion software suggests that the U.S. marketplace is more viable at this time. [Ch. 8: Accessibility—the firm must be able to reach members of the targeted segment.] Within this marketplace, e-motion software will focus on companies that have between 500 and 10,000 employees. These are the small-to-midsize companies that utilize the Oracle E-Business Suite of Applications. Companies of this size are unlikely to have their own development staffs in place or have the desire to develop and/or support home-grown applications. [Ch. 8: Responsiveness—the targeted market must respond to the marketing mix offered by the company.] Within these small-to-midsize companies, the individual target customer varies by the product offering. For example, a database administrator will be targeted for the company's system administrator products, and the IT director will be targeted for the functional line of product offerings.

Marketing Mix

[Ch. 2: Marketing mix (the four Ps) refers to the unique blend of product, place (distribution), promotion, and pricing strategies.]

Product

[Ch. 7: E-motion software provides a business service to its customers.]

E-motion software develops applications specifically for the Oracle E-Business Suite. For clients of Oracle Applications who desire greater efficiency and an increase in ROI on their installed ERP systems, e-motion software will offer a line of products designed specifically to improve performance of the existing Oracle Application installation. Clients that have in-house development staff will be able to lower the total cost of ownership of a product by having e-motion software upgrade their Oracle installation. [Ch. 7: The buying center includes all persons in an organization who become involved in the purchase decision. In-house development staff will play a critical role in the buying process.] Clients without in-house staff, however, are more likely to benefit from e-motion software installations because they will now be able to perform a greater number of tasks that are not offered by Oracle. [Ch. 7: In this instance, the members of the buying center are different from a company with an in-house development staff.]

As a product-based company, e-motion software cannot ignore the importance of product marketing. The three product attributes that will drive the business are level of service, usability, and clear return on purchase price. [Ch. 7: Quality, service, and price are important evaluative criteria in a purchase decision involving software products.] The reluctance of some customers to install relatively new third-party products into their ERP systems is an obstacle to overcome via product marketing. [Ch. 7: This is often a new buy for the customer.] The company has to deliver on the promise of the products—that promise being that "e-motion software products make the business process of our customers more efficient, while easily understanding the upgrades to the underlying Oracle Application." E-motion must remain focused on this promise during both the product development and the product delivery process. [Ch. 7: Keeping current customers satisfied is just as important as attracting new ones.]

E-motion software's product line consists of functions that respond to inefficiencies identified from years of experience with Oracle ERP systems. Since the product portfolio is built expressly for the Oracle Applications E-Business Suite, the products are updated continually to maintain compatibility as well as to take advantage of new technologies and capabilities released by Oracle. [Ch. 10: Quality and functional modifications keep e-motion software's products up-to-date with ongoing technological changes.] All products enjoy the following characteristics: tight integration with Oracle, intuitive design, compatible architecture, and streamlined interfaces. Product offerings are iPraise, Responsibility Management, Password Reset, and Global Directory. [Ch. 10: E-motion software's product mix width is comprised of one product—enterprise software. This product line is comprised of four product items.]

iPraise: [Ch. 10: IPraise is an individual brand.] The employee appraisal system developed by e-motion software is the most dynamic appraisal system available to Oracle customers. Combining e-motion software's commitment to streamlined application interfaces with the vast functionality available to Oracle E-Business Suite customers, iPraise represents the next generation of appraisal systems. The system is flexible, allowing it to be configured to meet the specific needs of the organization. Using the appraisal configuration engine, the customer can choose to include or omit several aspects of the appraisal process and even determine in which order they are to be constructed. Thus, iPraise is a complete solution for Oracle customers. Customers can opt to integrate other modules of Oracle that have been configured previously with the E-Business Suite. Installing iPraise is fast and easy.

Responsibility Management: [Ch. 10: Responsibility Management is an individual brand.] Responsibility Management solves one of the most important questions faced by all Oracle system administrators: "Who has access to which data?" Using Responsibility Management, a system administrator or database administrator can quickly, easily, and accurately identify who has access to which data in real time. Responsibility Management can inform the administrator of the following:

- Employees with particular responsibility
- Employees without a single responsibility
- User names that are not attached to any employee
- User names that are attached to more than one employee
- User accounts that are expiring in *x* number of days
- User accounts created in x days prior
- All users that have been given *y* responsibilities in *x* days prior

Results are displayed in a simple table that can be arranged and sorted. The table can also be exported to Excel for further investigation.

In addition to the query capabilities, Responsibility Management enables the system administrator to make changes to the user account, such as:

- End date a responsibility
- User account expiration update for a particular responsibility
- Bulk assignment of responsibilities (by organization, job, location, etc.)
- Bulk end-dating of responsibilities (by organization, job, location, etc.)

Overall, Responsibility Management enables system administrators to enforce security policies by providing a simple, easy-to-use function to identify who has what responsibility. Each day that a person has access not identified with his or her position is unnecessary and insecure.

Password Reset: [Ch. 10: Password Reset is an individual brand.] Forgotten passwords are the single largest end-user issue. Every day, help desks are bombarded with calls from end-users who have forgotten their passwords. The standard Oracle log-in link does not provide a solution for this problem; thus, end-users are forced to call the help desk to reset the password. E-motion software's Password Reset function is the solution.

Password Reset is modeled after the standard password reset functionality available on most Web sites. Even if the user is using Password Reset for the first time, all the components will seem familiar and the user will know where to go next without receiving complex instructions or training. Password Reset functions as a part of the Oracle Applications. There are not outside Web sites to access or other applications to open. The user simply clicks on a link from the login page, enters the required information, and the password is reset. The user can then login immediately with the new password. Password Reset validates a user's identity by going directly to the Oracle database and running queries against it. This tight integration ensures reliability.

Global Directory: [Ch. 10: Global Directory is an individual brand.] Most companies utilize a separate system for their corporate directory. This requires entering and maintaining all employee information in Oracle and then re-entering that information into a separate system. Worse yet, they print the company directory from a separate system. Not only is this extremely inefficient, but there is a greater chance for error. In today's fast changing world, employee information can change on a weekly basis. As a result, the "other" system is often neglected and its data are unreliable. Global Directory solves this issue by "going to source" and gathering data directly from the Oracle database; thus Global Directory has up-to-the-minute validity. Global Directory allows users to query the database for a wide variety of information. The results can be customized to give your employees the depth of knowledge they require.

Global Directory functions as part of the Oracle Applications. There are no outside Web sites to access or other applications to open. Using the export function, users can transfer results into Excel, XML, or CSV, making it possible to utilize the information for such items as contact lists, distribution forms, and mailing labels.

Place/Distribution

E-motion software is now headquartered in Bedford, Massachusetts. However, home office location has little to do with the actual distribution of e-motion software's products since the products are installed and implemented at the client company. E-motion software will perform its own marketing channel functions (e.g., transactional, logistical, and facilitating) and does not foresee the need for any intermediaries in this process. [Ch. 13: Channel members facilitate the exchange between buyer and seller. E-motion software is the only channel member engaged in getting its product to the customer. Thus, it uses a direct channel.] However, e-motion software is a strong supporter of industry groups, such as the Oracle Applications User Group, and related industry events. Such support allows the company to become recognized as a vendor among Oracle Applications clients.

E-motion software does offer a partner program for companies that wish to resell or refer e-motion software products to Oracle ERP clients. The program is segmented into two separate categories. The Alliance Partner Referral Program is tailored for businesses that have customer relationships with companies in specific industries or with businesses or IT needs that e-motion software programs can uniquely address. An Alliance Partner will identify e-motion software customers and refer them to e-motion software for a revenue share of the revenue from the referred account. As part of the program, Alliance Partner members receive all the training and materials needed to promote e-motion software solutions to their client base. The Alliance Solution Provider Program is designed for qualified Oracle-focused consultancies with a strong track record for providing top notch service to their clients. Partner program members are trained and certified by e-motion software. Once certified, implementation partners can then configure and implement e-motion software products with unparalleled service and support. [Ch. 13: This is a form of a strategic channel alliance for e-motion software.]

Promotion

[Ch. 16: E-motion software strives for integrated marketing communications.]
As a third party purveyor of products for Oracle, it is important for e-motion software to convey, clearly and succinctly, its "reason for being." Company material will have the heading: "e-motion software: we keep the business of business moving." [Ch. 17: This is the company's unique selling proposition.] We will emphasize the Oracle connection with the following statement on documents, as appropriate: "Oracle clients around the country are realizing true gains in productivity and efficiency by taking every day tasks and putting them in *motion*."

E-motion software will adhere to mainstream thinking regarding the promotion of third-party products for ERP solutions. [Ch. 16: As a complex buying decision, personal selling and strong print are effective methods for reaching potential customers.]

- A cohesive, easy-to-maneuver, and user-friendly Web site (**http://www.e-motionsoftware.com**) [Ch. 17: Company Web sites can be used to introduce new products, promote existing products, obtain consumer feedback, post news releases, etc.]
- Recorded demos on the company Web site (requires users to register for a demo user account) [Ch. 21: Registration is important for customer relationship management.]
- Press releases as a member of the Certified Oracle Partner Network [Ch. 17: Public relations is an important element of the promotional mix. Press releases can place positive information in the news media to attract attention to e-motion software.]
- Demonstrations presented at trade shows and events [Ch. 18: Trade promotions push a product through the distribution channel and are popular among business marketers. Trade shows and events are an important aspect of sales promotions.]
- Word-of-mouth and reference sites [Ch. 18: Referrals are a good source for leads in the personal selling process.]

Product Pricing Sheet

	License Price	Software Update & Support	Licensing Metric	Minimum
Application Infrastructure				
Password Reset	$15,000	$2,700/year	Enterprise	N/A
Responsibility Management	$6	18 percent/year	User	2,000
User Application				
iPraise	$10	18 percent/year	User	2,000
Corporate Information				
Global Directory	$2	18 percent/year	User	2,000

- The Internet via Google AdWords campaigns to drive potential clients to the company Web site [Ch. 17: The Internet has changed the advertising industry. Popular Internet sites sell advertising space to marketers, and search engine advertising is a popular approach.]
- Product datasheets that provide pertinent product data, features, and benefits of installation (available on the company W eb site or via hard copy) [Ch. 18: Product information is critical in the sales process.]

Importantly, e-motion software is a company that relies heavily on direct selling to reach potential customers. [Ch. 18: Producers of most business goods rely more heavily on personal selling than advertising. Informative personal selling is common for installations such as those offered by e-motion software.] This promotional method requires a large amount of cold calling. [Ch. 18: Personal selling is important when a product has high value and is technically complex. Relationship selling, or consultative selling, builds long-term relationships with clients.] E-motion software purchases the names of potential customers from marketing services that collect such information from customers of Oracle ERP products [Ch. 18: Generating leads is the first step in the selling process.]

Price

E-motion software prices its products to sufficiently cover the costs associated with development, sales, and support and to provide cash flow for future growth and development. [Ch. 19: As a new company, e-motion software is very concerned about covering its costs and having money left over for investment into the business. While not stated exactly, it appears that the company has a profit-oriented pricing objective.] The following table provides the company's standard price list. These list prices can vary, however, as there is a trickle-down effect in the industry. Essentially, pricing starts with Oracle, trickles through the consulting firm, and then down to e-motion products.

Prices are based on industry standards for classification. [Ch. 20: Status quo pricing is when a company meets the competition or going rate pricing. It appears that e-motion software is using status quo logic in its price setting.] For example, Password Reset, as an enterprise system product, has a total purchase price of $15,000, with a $2,700 software update and support fee. [Ch. 20: Two-part pricing is when the company charges two separate amounts for the product. In this instance, the buyer pays the $15,000 for the enterprise system product and then pays another $2,700 for the update and fee.] Responsibility Management, iPraise, and Global Directory are priced on a per employee (user) basis with a minimum purchase of 2,000 employees. For example, Global Directory is $2 per employee with a minimum purchase of 2,000 employees. Thus, the least amount a company could purchase this product for is $4,000. The 18 percent annual maintenance fee is the industry standard. [Ch. 20: This shows the two-part, status quo pricing.]

VI IMPLEMENTATION, EVALUATION, AND CONTROL

Marketing Research

The company needs to keep abreast of two distinct segments in the marketplace: its client needs and Oracle's direction. E-motion software needs to understand its clients and their ongoing needs. [Ch. 21: E-motion software captures customer data, storing and integrating it into a customer database.] This includes meeting current needs and forecasting future needs as the Oracle Application Suite continues to evolve. E-motion software must also maintain up-to-date and accurate intelligence on both current Oracle offerings and planned initiatives. [Ch. 9: Ongoing marketing research will help the company keep abreast of what is happening in the marketplace.] By doing this, it will be able to introduce products that complement new Oracle functions and will be less likely to offer products that compete for functions that are included at no charge in an Oracle license. Additionally, this will present opportunities to introduce products that complement new Oracle functionality.

Organizational Structure and Plan

As a start-up company, e-motion software currently has only one member on its staff, Scott Keohane. As e-motion software matures into a stable, profitable organization, the need for employees will grow. The first foreseeable employee need is in the area of sales. The plan is to hire a sales person in early 2006 to allow Mr. Keohane can continue his consulting on a regular basis, while at the same time ensuring a steady supply of funds for continued development efforts. To obtain the financial flexibility it needs to manage its cash flow successfully, the company has made contractors a significant component of its workforce. Contractors are used in the following areas: application development, database administration, and marketing. Current contractors have been associated with e-motion software almost since the company's inception and are largely credited with its early successes.

To provide a management resource from which Keohane can receive regular advice and guidance, e-motion software has assembled a nonvoting, nonbinding advisory council to assist in decision making, overall strategy, and execution. The advisory council is composed of four outside members who have made a commitment to provide their expertise and experience, free of charge, to e-motion software. Advisory members interact quarterly via teleconference.

Financial Projections

[Ch. 2: Evaluation and control are important mechanisms for monitoring the effectiveness of the marketing plan. Financial objectives are a common measure of success/failure.]

The financial objective is to be financially solvent within the first two years of operation.

Objective Metric: Sales of $250,000 by the end of 2005
Sales of $2 million by the end of 2007
Gross margin higher than 80 percent
Positive cash flow yearly

[Ch. 2: Stated objectives must be measurable and time specific.]

The five-year financial projection plan (in U.S. dollars) for e-motion software is:

Five years financial projection plan

	2006	2007	2008	2009	2010
Revenues:					
iPraise	$50,000	$100,000	$600,000	$2,225,000	$5,500,000
Responsibility Mgt	60,000	80,000	160,000	420,000	700,000
Password Reset	225,000	180,000	180,000	150,000	75,000
Global Directory	45,000	75,000	180,000	300,000	465,000
Cost of Goods Sold	0	0	0	0	0
General & Administrative	$350,000	$765,000	$1,600,000	$2,165,000	$2,600,000

Implementation Timetable

[Ch. 2: Implementation is the process that turns a marketing plan into action assignments and ensures that these assignments are executed appropriately.]

2005

- The company plans to have three major Oracle clients by the end of 2005.

2006

- The company plans to have secured at least one client in each region of the United States by the end of 2006. This would mean at least one customer in the Northeast, the Mid-Atlantic, the Southeast, the Midwest, the Northwest, and the West Coast.
- Keohane plans to hire one full-time salesperson.

Summary

E-motion software continually monitors activities with current and potential clients. As a consultant in the industry, Keohane is always on the lookout for potential clients. He has set quarterly and yearly sales targets, and actual sales will be compared to these quarterly plans. Additionally, Keohane will continue in his efforts to enlist at least one client in each of the major geographic regions of the United States. However, it may take a qualified salesperson to devote the time necessary to acquire new customers.

Additionally, by not being restricted to Keohane's current consultancies, a dedicated salesperson could more readily identify potential e-motion software clients by not being restricted to current consultancies that Keohane is involved with. Of major concern is that the current financial strategy of supporting the new business by personal funds from consulting may prove to be too onerous for Keohane.

Ultimately, the goal is to 'make it big.' The hope is that, over the next five years, the small products that e-motion software has developed will hopefully generate cash sufficient to build a larger module that one of the larger ERP companies (e.g., Oracle) will want to acquire.

Ethics and Social Responsibility

CHAPTER 3

Learning Outcomes

- LO 1 Explain the determinants of a civil society
- LO 2 Explain the concept of ethical behavior
- LO 3 Describe ethical behavior in business
- LO 4 Discuss corporate social responsibility
- LO 5 Describe the arguments for and against social responsibility
- LO 6 Explain cause-related marketing

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John Mackey, CEO of the Whole Foods Market, went online using the screen name "rahodeb" (a scramble of Deborah, his wife's name) and attacked competitor Wild Oats Markets on Yahoo! He said the smaller company was "mediocre with a terrible track record." William Swanson, Chairman and CEO of Raytheon, wrote a book entitled *Swanson's Unwritten Rules of Management*. It was later discovered the book contained passages that exactly mirrored a 1944 book by an engineering professor. David Edmondson, former CEO of RadioShack, claimed to have degrees in theology and psychology, but completed only two semesters of course work.[1] And the list could go on.

The activities of these top managers were clearly wrong. Yet for several thousand years religious teaching and secular ethics have sought to encourage socially beneficial behavior. The literature of virtually every religious tradition, as well as Eastern and Western philosophy, are full of examples, rules, and guidance regarding what constitutes right and wrong.

LO 1

Determinants of a Civilized Society[2]

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Have you ever stopped and thought about the social glue that binds society together? That is, what factors are in place that keep people and organizations from running amuck and doing harm, and what factors create order in a society like ours as opposed to chaos. The six modes of social control are listed below:

1. *Ethics:* The first is ethical rules and guidelines along with customs and traditions that provide principles of right action.
2. *Laws:* Often rules and guidelines are codified into law. Laws created by governments are then enforced by governmental authority. Thus, the dictum, "Thou shall not steal," is part of formal law throughout the land. Law, however, is not a perfect mechanism for ensuring good corporate and employee behavior. This is because laws often address the lowest common denominator of socially acceptable behavior. In other words, just because something is not illegal doesn't mean that it is right. For example, an individual goes to Barnes and Noble everyday and spends the afternoon reading books and magazines in the store. The store has big comfortable chairs and the clerks never bother him or ask him to leave. He even takes his own lunch if he plans to spend the day there. He does this at least 20 days per month. The bookstore allows this practice and it is not against the law. It is, however, not ethical. If everyone who bought books followed this individual's behavior, Barnes and Noble would soon be bankrupt!
3. *Formal and Informal Groups:* Businesses, professional organizations (such as the American Marketing Association), clubs

Marketing & You

Using the following scale, enter the numbers that reflect your opinions.

1 2 3 4 5 6 7 8 9

Completely disagree — Completely agree

— The ethics and social responsibility of a firm are essential to its long-term profitability.

— Business ethics and social responsibility are critical to the survival of a business enterprise.

— The overall effectiveness of a business can be determined to a great extent by the degree to which it is ethical and socially responsible.

— Good ethics is often good business.

— Business has a social responsibility beyond making a profit.

— Corporate planning and goal-setting sessions should include discussions of ethics and social responsibility.

— Social responsibility and profitability can be compatible.

Now, total your score. Find out what it means after you read the chapter.

(e.g., Shriners or Ducks Unlimited), and professional associations (e.g., American Medical Association), all have codes of conduct. These codes prescribe acceptable and desired behaviors of their members.

4. *Self regulation:* Self regulation involves the voluntary acceptance of standards established by nongovernmental entities such as the American Association of Advertising Agencies (AAAA) or the American Manufacturers Association. The AAAA has a self-regulation arm that deals with deceptive advertising. Other associations have regulations relating to child labor, environmental issues, conservation, and a host of other issues.

5. *The Media:* In an open, democratic society, the media play a key role in informing the public about actions of individuals and organizations. These stories sometimes praise, such as the media coverage of Wal-Mart's efforts to help people and reopen stores after Hurricane Katrina. Or shine the spotlight on unscrupulous behavior such as those of Enron and Worldcom. Business firms dislike negative publicity, which can lead to lost sales, damage to corporate reputations, government actions, and legal liability. Conversely, favorable publicity stimulates sales and builds the firm's reputation.

6. *An Active Civil Society:* An informed and engaged society can help shape and mold individual and corporate behavior. The last state in the union to get a Wal-Mart store was Vermont. Citizen campaigns against the big-box retailer were deciding factors in management's decision to avoid the state. When pro football player Michael Vick was convicted of dog fighting, a grass roots campaign sprang up to boycott Nike. Vick had an endorsement contract with the shoe manufacturer.

All six factors above individually and in combination are critical to achieving a socially coherent, vibrant, civilized society. These six factors (the social glue) are more important today than ever before due to the increasing complexity of the global economy and the melding of customs and traditions within societies.

REVIEW LEARNING OUTCOME

LO 1 Explain the determinants of a civilized society.

LO 2
The Concept of Ethical Behavior

It has been said that ethics is something everyone likes to talk about but nobody knows exactly what it is. Others have noted that "defining ethics is like trying to nail Jello to the wall. You begin to think that you understand it, but that's when it starts squirting out between your fingers."

ethics
The moral principles or values that generally govern the conduct of an individual.

Ethics refers to the moral principles or values that generally govern the conduct of an individual or a group. Ethics also can be viewed as the standard of behavior by which conduct is judged. As noted above, standards that are legal may not always be ethical, and vice versa. Laws are the values and standards enforceable by the courts. Ethics, then, consists of personal moral principles. For example, there is no legal statute that makes it a crime for someone to "cut in line." If someone doesn't want to wait in line and cuts to the front, it often makes others very angry. We sneer at drivers who sneak along the side of the road to get around a line of traffic as we sit and wait our turn.

If you have ever resented a line-cutter, then you understand ethics and have applied ethical standards in life. Waiting your turn in line is an expectation society has.

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"Waiting your turn" is not an ordinance, a statute, or even a federal regulation. "Waiting your turn" is an age-old principle developed because it was fair to proceed with first-in-time, first to be served. "Waiting your turn" exists because when there are large groups waiting for the same road, theater tickets, or fast food at noon in a busy downtown area, we found that lines ensured order and that waiting your turn was a just way of allocating the limited space and time allotted for the movie tickets, the traffic, or the food. "Waiting your turn" is an expected but unwritten behavior that plays a critical role in an orderly society.[3]

So it is with ethics. Ethics consists of those unwritten rules we have developed for our interactions with each other. These unwritten rules govern us when we are sharing resources or honoring contracts. "Waiting your turn" is a higher standard than the laws that are passed to maintain order. Those laws apply when physical force or threats are used to push to the front of the line. Assault, battery, and threats are forms of criminal conduct for which the offender can be prosecuted. But the law does not apply to the stealth line-cutter who simply sneaks to the front, perhaps using a friend and a conversation as a decoy for edging into the front. No laws are broken, but the notions of fairness and justice are offended by one individual putting himself above others and taking advantage of others' time and position.[4]

When you say to yourself, "That's unjust!" "That's unfair!" you have just defined ethics for yourself! Ethics is not just about standards of behavior; ethics is about honesty, justice and fairness. This is true for both personal and business behavior.

Ethical questions range from practical, narrowly defined issues, such as a business person's obligation to be honest with his customers, to broader social and philosophical questions, such as a company's responsibility to preserve the environment and protect employee rights. Many ethical conflicts develop from conflicts between the differing interests of company owners and their workers, customers, and surrounding community. Managers must balance the ideal against the practical—the need to produce a reasonable profit for the company's shareholders with honesty in business practices, and larger environmental and social issues.

ETHICAL THEORIES

People usually base their individual choice of ethical theory on their life experiences. The following are some of the ethical theories that apply to marketing.[5]

Deontology The deontological theory states that people should adhere to their obligations and duties when analyzing an ethical dilemma. This means that a person will follow his or her obligations to another individual or society because upholding one's duty is what is considered ethically correct. For instance, a deontologist will always keep his promises to a friend and will follow the law. A person who follows this theory will produce very consistent decisions since they will be based on the individual's set duties. Note that this theory is not necessarily concerned with the welfare of others. Say, for example, a sales person has decided that it's his ethical duty (and very practical!) to always be on time to meetings with clients. Today he is running late. How is he supposed to drive? Is the deontologist supposed to speed, breaking the law to uphold his duty to society, or is the deontologist supposed to arrive at his meeting late, breaking his duty to be on time? This scenario of conflicting obligations does not lead us to a clear ethically correct resolution, nor does it protect the welfare of others from the deontologist's decision.

deontological theory
A theory that states that people should adhere to their obligations and duties when analyzing an ethical dilemma.

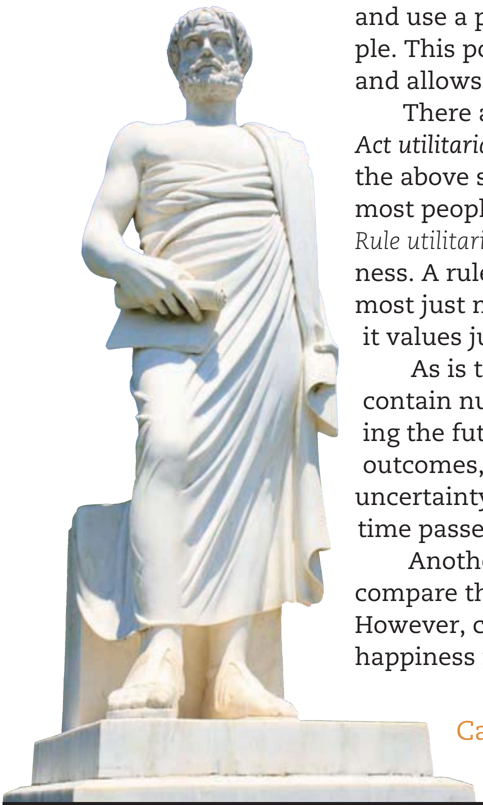
utilitarian ethical theory
A theory that holds that the choice that yields the greatest benefit to the most people is the choice that is ethically correct.

Utilitarianism The utilitarian ethical theory is founded on the ability to predict the consequences of an action. To a utilitarian, the choice that yields the greatest benefit to the most people is the choice that is ethically correct. One benefit of this ethical theory is that the utilitarian can compare similar predicted solutions and use a point system to determine which choice is more beneficial for more people. This point system provides a logical and rational argument for each decision and allows a person to use it on a case-by-case context.

There are two types of utilitarianism: act utilitarianism and rule utilitarianism. *Act utilitarianism* adheres exactly to the definition of utilitarianism as described in the above section. In act utilitarianism, a person performs the acts that benefit the most people, regardless of personal feelings or the societal constraints such as laws. *Rule utilitarianism*, however, takes into account the law and is concerned with fairness. A rule utilitarian seeks to benefit the most people but through the fairest and most just means available. Therefore, added benefits of rule utilitarianism are that it values justice and doing good at the same time.

As is true of all ethical theories, however, both act and rule utilitarianism contain numerous flaws. Inherent in both are the flaws associated with predicting the future. Although people can use their life experiences to attempt to predict outcomes, no human being can be certain that his predictions will be true. This uncertainty can lead to unexpected results, making the utilitarian look unethical as time passes because his choice did not benefit the most people as he predicted.

Another assumption that a utilitarian must make is that he has the ability to compare the various types of consequences against each other on a similar scale. However, comparing material gains such as money against intangible gains such as happiness is impossible since their qualities differ so greatly.



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Aristotle and Plato taught that solving ethical dilemmas requires training, that individuals solve ethical dilemmas when they develop and nurture a set of virtues.

Casuist The **casuist ethical theory** compares a current ethical dilemma with examples of similar ethical dilemmas and their outcomes. This allows one to determine the severity of the situation and to create the best possible solution according to others' experiences. Usually, one will find examples that represent the extremes of the situation so that a compromise can be reached that will hopefully include the wisdom gained from the previous situations.

One drawback to this ethical theory is that there may not be a set of similar examples for a given ethical dilemma. Perhaps that which is controversial and ethically questionable is new and unexpected. Along the same line of thinking, this theory assumes that the results of the current ethical dilemma will be similar to results in the examples. This may not be necessarily true and would greatly hinder the effectiveness of applying this ethical theory.

casuist ethical theory
A theory that compares a current ethical dilemma with examples of similar ethical dilemmas and their outcomes.

moral relativists
Persons who believe that ethical truths depend on the individuals and groups holding them.

virtue
A character trait valued as being good.

Moral Relativists[6] **Moral relativists** believe in time-and-place ethics, i.e., ethical truths depend on the individuals and groups holding them. Arson is not always wrong in their book. If you live in a neighborhood in which drug dealers are operating a crystal meth lab or crack house, arson is ethically justified. If you are a parent and your child is starving, stealing a loaf of bread is ethically correct. The proper resolution to ethical dilemmas is based upon weighing the competing factors at the moment and then making a determination to take the lesser of the evils as the resolution. Moral relativists do not believe in absolute rules. Their beliefs center on the pressure of the moment and whether the pressure justifies the action taken.

REVIEW LEARNING OUTCOME

LO 2 Explain the concept of ethical behavior.

Ethical conflicts for business owners, managers, customers, workers, and the communities can sometimes be resolved through the reliance on ethical theories such as deontology, utilitarianism, casuist, moral relativism, and virtue ethics.

Virtue Ethics[7] Aristotle and Plato taught that solving ethical dilemmas requires training, that individuals solve ethical dilemmas when they develop and nurture a set of virtues. A **virtue** is a character trait valued as being good. Aristotle taught the importance of cultivating virtue in his students and then having them solve ethical

Exhibit 3.1

Standards for Being Virtuous

Virtue standard	Definition	Virtue standard	Definition
Ability	being dependable and competent	Humility	giving proper credit
Acceptance	making the best of a bad situation	Humor	bringing relief; making the world better
Amiability	fostering agreeable social contexts	Independence	getting things done despite bureaucracy
Articulateness	ability to make and defend one's case	Integrity	being a model of trustworthiness
Attentiveness	listening and understanding	Justice	treating others fairly
Autonomy	having a personal identity	Loyalty	working for the well-being of an organization
Caring	worrying about the well-being of others despite power	Pride	being admired by others
Charisma	inspiring others	Prudence	minimizing company and personal losses
Compassion	sympathetic	Responsibility	doing what it takes to do the right thing
Coolheadedness	retaining control and reasonableness in heated situations	Saintliness	approaching the ideal in behavior
Courage	doing the right thing despite the cost	Shame (capable of)	regaining acceptance after wrong behavior
Determination	seeing a task through to completion	Spirit	appreciating a larger picture in situations
Fairness	giving others their due; creating harmony	Toughness	maintaining one's position
Generosity	sharing, enhancing others' well-being	Trust	dependable
Graciousness	establishing a congenial environment	Trustworthiness	fulfilling one's responsibilities
Gratitude	giving proper credit	Wittiness	lightening the conversation when warranted
Heroism	doing the right thing despite the consequences	Zeal	getting the job done right; enthusiasm
Honesty	telling the truth; not lying		

SOURCE: From Robert C. Solomon, "A Better Way to Think About Business: How Personal Integrity Leads to Corporate Success" (New York: Oxford University Press, 2003) p. 18. Used by permission of Oxford University Press, Inc.

dilemmas using those virtues once they had become an integral part of their being through their virtue training.

Some modern philosophers have embraced this notion of virtue and have developed lists of what constitutes a virtuous business person. Exhibit 3.1 reveals a list of virtuous standards.

LO3
Ethical Behavior in Business

Depending upon which, if any, ethical theory a businessperson has accepted and uses in his/her daily conduct, the action taken may vary. For example, faced with bribing a foreign official to get a critically needed contract or shutting down a factory and laying off a thousand workers, a person following a deontology strategy would not pay the bribe. Why? A deontologist always follows the law. However, a moral relativist will probably pay the bribe.

While the boundaries of what is legal and what is not are often fairly clear, e.g., don't run a red light, don't steal money from a bank, and don't kill someone, the boundaries of ethical decision making are predicated on which ethical theory one is following. The law typically relies on juries to determine if an act is legal or illegal. Society determines whether an action is ethical or unethical. Sometimes society decides that a person acted unethically—think O.J. Simpson—but a jury may decide that no illegal act was committed. In a business-related case, a jury

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Sometimes society decides that a person acted unethically but a jury may decide that no illegal act was committed.

recently found Richard Scrushy, charged with a $1.4 billion fraud at HealthSouth Corporation, innocent on all counts. On the other hand, Bernard Ebbers, former CEO of WorldCom, was found guilty of securities fraud and filing false documents and was sentenced to 25 years in prison.

Morals are the rules people develop as a result of cultural values and norms. Culture is a socializing force that dictates what is right and wrong. Moral standards may also reflect the laws and regulations that affect social and economic behavior. Thus, morals can be considered a foundation of ethical behavior.

morals
The rules people develop as a result of cultural values and norms.

Morals are usually characterized as good or bad. "Good" and "bad" have different connotations, including "effective" and "ineffective." A good salesperson makes or exceeds the assigned quota. If the salesperson sells a new stereo or television set to a disadvantaged consumer—knowing full well that the person can't keep up the monthly payments—is the salesperson still a good one? What if the sale enables the salesperson to exceed his or her quota?

"Good" and "bad" can also refer to "conforming" and "deviant" behaviors. A doctor who runs large ads offering discounts on open-heart surgery would be considered bad, or unprofessional, in the sense of not conforming to the norms of the medical profession. "Bad" and "good" are also used to express the distinction between criminal and law-abiding behavior. And finally, different religions define "good" and "bad" in markedly different ways. A Muslim who eats pork would be considered bad, as would a fundamentalist Christian who drinks whiskey.

MORALITY AND BUSINESS ETHICS

Today's business ethics actually consist of a subset of major life values learned since birth. The values businesspeople use to make decisions have been acquired through family, educational, and religious institutions.

Ethical values are situation specific and time oriented. Nevertheless, everyone must have an ethical base that applies to conduct in the business world and in personal life. One approach to developing a personal set of ethics is to examine the consequences of a particular act. Who is helped or hurt? How long lasting are the consequences? What actions produce the greatest good for the greatest number of people? A second approach stresses the importance of rules. Rules come in the form of customs, laws, professional standards, and common sense. Consider these examples of rules:

- Always treat others as you would like to be treated.
- Copying copyrighted computer software is against the law.
- It is wrong to lie, bribe, or exploit.

Another approach emphasizes the development of moral character within individuals. Ethical development can be thought of as having three levels:[8]

- *Preconventional morality*, the most basic level, is childlike. It is calculating, self-centered, and even selfish, based on what will be immediately punished or rewarded. Fortunately, most businesspeople have progressed beyond the self-centered and manipulative actions of preconventional morality.
- *Conventional morality* moves from an egocentric viewpoint toward the expectations of society. Loyalty and obedience to the organization (or society) become paramount. At the level of conventional morality, a marketing decision maker would be concerned only with whether the proposed action is legal and how it

Exhibit 3.2

Unethical Practices Marketing Managers May Have to Deal With

- Entertainment and gift giving
- False or misleading advertising
- Misrepresentation of goods, services, or company capabilities
- Lying to customers in order to get the sale
- Manipulation of data (falsifying or misusing statistics or information)
- Misleading product or service warranties
- Unfair manipulation of customers
- Exploitation of children or disadvantaged groups
- Stereotypical portrayals of women, minority groups, or senior citizens
- Invasion of customer privacy
- Sexually oriented advertising appeals
- Product or service deception
- Unsafe products or services
- Price deception
- Price discrimination
- Unfair or inaccurate statements about competitors
- Smaller amounts of product in the same-size packages

will be viewed by others. This type of morality could be likened to the adage "When in Rome, do as the Romans do."

- *Postconventional morality* represents the morality of the mature adult. At this level, people are less concerned about how others might see them and more concerned about how they see and judge themselves over the long run. A marketing decision maker who has attained a postconventional level of morality might ask, "Even though it is legal and will increase company profits, is it right in the long run? Might it do more harm than good in the end?"

ETHICAL DECISION MAKING

How do businesspeople make ethical decisions? There is no cut-and-dried answer. Some of the ethical issues managers face are shown in Exhibit 3.2. Studies show that the following factors tend to influence ethical decision making and judgments:[9]

- *Extent of ethical problems within the organization:* Marketing professionals who perceive fewer ethical problems in their organizations tend to disapprove more strongly of "unethical" or questionable practices than those who perceive more ethical problems. Apparently, the healthier the ethical environment, the more likely that marketers will take a strong stand against questionable practices.
- *Top-management actions on ethics*: Top managers can influence the behavior of marketing professionals by encouraging ethical behavior and discouraging unethical behavior. Research found that 13 percent of large-company top executives thought that having strong ethical traits was the most important leadership trait of CEOs. That is down from 20 percent in 2003.[10] The most important trait to the majority of respondents was the ability to inspire others (37 percent).[11] Other research found three ethics-related actions by managers have the greatest impact on employee ethics. These are: setting a good example, keeping promises and commitments, and supporting others in adhering to ethics standards.[12]
- *Potential magnitude of the consequences*: The greater the harm done to victims, the more likely that marketing professionals will recognize a problem as unethical.
- *Social consensus*: The greater the degree of agreement among managerial peers that an action is harmful, the more likely that marketers will recognize a problem as unethical.
- *Probability of a harmful outcome*: The greater the likelihood that an action will result in a harmful outcome, the more likely that marketers will recognize a problem as unethical.
- *Length of time between the decision and the onset of consequences*: The shorter the length of time between the action and the onset of negative consequences, the more likely that marketers will perceive a problem as unethical.

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In order to comply with new human rights policies, police in Northern Ireland will not be issued with controversial Taser stun guns in the immediate future.

- *Number of people to be affected*: The greater the number of persons affected by a negative outcome, the more likely that marketers will recognize a problem as unethical.

As you can see, many factors determine the nature of ethical decision making. An example is Taser International Inc., the world's largest maker of stun guns. Management talks tough when the subject turns to people who've sued the company for injuries or deaths allegedly inflicted by electric shock from its weapons. The word has gotten out: Taser doesn't settle. Taser General Counsel Doug Klint said, "Anyone who sues us is in for a fight." Taser's stun gun, sold mainly to police departments, fires two insulated conductive wires with barbs at the end as far as 35 feet, delivering a 50,000-volt jolt that temporarily paralyzes the target. Taser's refusal to settle personal-injury or wrongful-death claims has resulted in fewer lawsuits being filed, Klint said. While about 50 suits are still pending, Taser has seen a "significant decline" in the rate of new litigation. "There was a lot of controversy in 2005, a lot of concerns about the safety of the product, but I think after 52 consecutive wins in court, we've laid the concerns to rest," Chief Executive Officer Rick Smith said in an interview. When asked whether the company considers settling, he said, "We like to litigate every one that we can."[13] Lawyers for alleged Taser victims say the company overstates its legal scoreboard to discourage lawsuits and boost its stock price. "They're trying to deter other litigants while making themselves look good to investors," said Las Vegas attorney E. Brent Bryson, who represents plaintiffs in two cases over Taser-related deaths.[14]

ETHICAL GUIDELINES AND TRAINING

Many organizations have become more interested in ethical issues. One sign of this interest is the increase in the number of large companies that appoint ethics officers—from virtually none a few years ago to almost 33 percent of large corporations now. More and more companies are providing ethics resources for their employees. Today over 70 percent of employees in the United States can seek advice on ethics questions via telephone, e-mail, Web, or in-person. (See **http://www.ethics.org** for more information.) In addition, many companies of various sizes have developed a code of ethics as a guideline to help marketing managers and other employees make better decisions. In fact, a national study found that 60 percent of companies surveyed had a code of ethics, 33 percent offered ethics training, and 33 percent employed an ethics officer.[15] Some of the most highly praised codes of ethics are those of Intel, IBM, Starbucks, and Costco.

code of ethics
A guideline to help marketing managers and other employees make better decisions.

Creating ethics guidelines has several advantages:

- The guidelines help employees identify what their firm recognizes as acceptable business practices.
- A code of ethics can be an effective internal control on behavior, which is more desirable than external controls like government regulation.
- A written code helps employees avoid confusion when determining whether their decisions are ethical.
- The process of formulating the code of ethics facilitates discussion among employees about what is right and wrong and ultimately leads to better decisions.

Exhibit 3.3

General Mills Code of Ethics

Times may change, but our values have endured. Honesty. Integrity. Trust. Our values are the source of our strength. They remain the heart of who we are and what we do.

For more than 130 years—since John S. Pillsbury and Cadwallader C. Washburn first began building their competing businesses along the Mississippi River—we have held our company and ourselves to the highest standards of ethical conduct and personal integrity.

We set very high expectations for ourselves—and for the integrity of our company. We will not compromise those standards.

- We strive for the highest quality in our products, services and relationships.
- We set and maintain the highest standards for all aspects of our work.
- We advance and grow our businesses honestly and ethically, taking no shortcuts that might compromise our high standards.
- We comply with local laws in every nation where we operate. We recognize and respect the cultures, customs and practices of our consumers and customers in nations around the world.
- We steer clear of conflicts of interest, and work to avoid even the perception of conflict.
- We deliver on our promises.
- We are ever mindful of the trust our consumers, customers, partners and employees place in General Mills. We will never knowingly or willfully undermine that trust.

SOURCE: General Mills

An example of a basic code of ethics is shown in Exhibit 3.3.

Businesses, however, must be careful not to make their code of ethics too vague or too detailed. Codes that are too vague give little or no guidance to employees in their day-to-day activities. Codes that are too detailed encourage employees to substitute rules for judgment. For instance, if employees are involved in questionable behavior, they may use the absence of a written rule as a reason to continue behaving that way, even though their conscience may be saying no. The checklist in Exhibit 3.4 is an example of a simple but helpful set of ethical guidelines. Following the checklist will not guarantee the "rightness" of a decision, but it will improve the chances that the decision will be ethical. Although many companies have issued policies on ethical behavior, marketing managers must still put the policies into effect. They must address the classic "matter of degree" issue. For example, marketing researchers must often resort to deception to obtain unbiased answers to their research questions. Asking for a few minutes of a respondent's time is dishonest if the researcher knows the interview will last 45 minutes. Not only must management post a code of ethics, but it must also give examples of what is ethical and unethical for each item in the code. Moreover, top management must stress to all employees the importance of adhering to the company's code of ethics. Without a detailed code of ethics and top management's support, creating ethical guidelines becomes an empty exercise.

Ethics Training Ethics training is a good way to help employees put good ethics into practice. Because of the numerous corporate scandals in the past decade, such as Enron, Tyco, Worldcom, Hewlett-Packard, and Adelphia Communications Corporation, more and more companies are offering ethics training to their employees. Today, about 70 percent of all large employers (over 500 employees) provide ethics training.[16] Simply giving employees a long list of "dos and don'ts" is a start, but doesn't really help navigate the gray areas. What is needed then is a more contextual approach to ethics training.

Lockheed Martin is one firm that has moved to contextual ethics training. Recently, Manny Zulueta met with seven colleagues to watch a DVD. In one scene, a worker complained to his manager's boss after the manager yelled at her workers.

Exhibit 3.4
Ethics Checklist

- Does the decision benefit one person or group but hurt or not benefit other individuals or groups? In other words, is my decision fair to all concerned?
- Would individuals or groups, particularly customers, be upset if they knew about my decision?
- Has important information been overlooked because my decision was made without input from other knowledgeable individuals or groups?
- Does my decision presume that my company is an exception to a common practice in this industry and that I therefore have the authority to break a rule?
- Would my decision offend or upset qualified job applicants?
- Will my decision create conflict between individuals or groups within the company?
- Will I have to pull rank or use coercion to implement my decision?
- Would I prefer to avoid the consequences of my decision?
- Did I avoid truthfully answering any of the above questions by telling myself that the risks of getting caught are low or that I could get away with the potentially unethical behavior?

The manager apologized, but the worker soon felt that the manager was retaliating by giving him lousy assignments, nitpicking his work, and reprimanding him for arriving late. Mr. Zulueta, Lockheed Martin's senior vice president of shared services, then led what he says was a "nuanced" discussion about the ethical issues involved in that scene. Zuelueta's colleagues rightly noted that they needed more information—they needed to put the scene in context—to discern whether the manager's actions were retaliatory.[17] Understanding the context of an ethical problem helps employees navigate the gray areas.

The Most Ethical Companies Each year, *Ethisphere* magazine (targeted toward top management and focused on ethical leadership) examines over 5000 companies in 30 separate industries seeking the world's most ethical companies. It then lists the top 100. The magazine uses a rigorous format to identify true ethical leadership. A few of the selected winners are shown in Exhibit 3.5.

CULTURAL DIFFERENCES IN ETHICS

Studies suggest that ethical beliefs vary only little from culture to culture. Certain practices, however, such as the use of illegal payments and bribes, are far more acceptable in some places than in others (see the Global Perspectives Box below). Some countries have a dual standard concerning illegal payments. For example, German businesspeople typically treat bribes as tax-deductible business expenses. In Russia, bribes and connections in the government are essential for doing business. For instance, bribing a public official is the fastest method for accomplishing bureaucratic tasks such as registering a business. What we call bribery is a natural way of doing business in some other cultures. Do these widespread practices suggest that global marketers should adopt a "When in Rome, do as the Romans do" mentality?

Yet another example of cultural differences is the Japanese reluctance to enforce their antitrust laws. Everyday business practices, from retail pricing to business structuring, ignore antitrust regulations against restraint of trade, monopolies, and price discrimination. Not surprisingly, the Japanese are tolerant of scandals involving antitrust violations, favoritism, price fixing, bribery, and other activities considered unethical in the United States.

Foreign Corrupt Practices Act
A law that prohibits U.S. corporations from making illegal payments to public officials of foreign governments to obtain business rights or to enhance their business dealings in those countries.

Concern about U.S. corporations' use of illegal payments and bribes in international business dealings led to passage of the Foreign Corrupt Practices Act. This act prohibits U.S. corporations from making illegal payments to public officials of foreign governments to obtain business rights or to enhance their business dealings

Exhibit 3.5

Selected Winners of the World's Most Ethical Companies Award

ALCOA

Perry Minis, Director of Global Ethics & Compliance

Perry Minis is the Director of Global Ethics & Compliance for Alcoa, a metals and mining company with over 120,000 employees in 44 countries. Minnis, who started with Alcoa in finance 39 years ago, runs the Global Ethics & Compliance department to track metrics and determine if the company has a positive impact on the community. According to Minnis, "Our management has a very strong focus on safety. Alcoa is considered to be one of the safest corporations in the world." The company's Ethics and Compliance Council, which includes the CEO, vice presidents, and department directors, was formed in order to notify all executives of the latest in operations. The Council presents findings to the Board on a quarterly basis.

Minnis notes that Alcoa's Code of Conduct has been condensed to apply to specific roles and translated into different languages in order to make it an effective tool for all employees. The Code is also provided to suppliers, so they understand Alcoa's expectations and policies. "If a vendor's values or policies differ drastically from Alcoa, chances are they won't be doing business with us," emphasizes Minnis. He continues, "The most important thing is our values. We have a set of values and policies that is consistent across the company, and we train all employees to adhere to and uphold those values."

EATON

Sandy Cutler, CEO

Sandy Cutler, CEO of Eaton Corporation, spoke in great detail about the basic beliefs that make Eaton a value-based company. These core values have allowed Eaton to maintain a strong foundation and sense of stability during recent internal changes and mergers. Rather than approaching ethics as a compliance issue, Cutler believes, "It's about doing business right through internal philosophies and customer commitments. We'll lose business before we will compromise our values."

Eaton employs 61,000 people in 125 countries, and almost all of their products are targeted at helping people and companies to effectively use energy. For example, Eaton developed a technology with the EPA for UPS that allowed the shipping company to save 70 percent in fuel economy. Additionally, Eaton developed a hybrid electric bus technology for possible use during the Beijing Olympics.

Eaton places high value on contributions in the workplace and community, believing they are key components for doing business right. "People will work where the company and the community involvement values reflect their own," insists Cutler. Every employee at Eaton has the opportunity to raise questions if they believe their personal morals are at risk. If a company is committed to doing business ethically, "you can cut the top off and the bottom would keep working," maintains Cutler.

JOHN DEERE

James R. Jenkins, Senior Vice President and General Counsel

In business for 170 years, John Deere prides itself on enabling "human flourishing." With core values of integrity, quality, innovation and commitment, the company provides advanced products and services for agriculture, forestry, construction and landscaping, as well as manufacturing engines for use in heavy equipment. James R. Jenkins, Senior VP and General Counsel for Deere & Company, said "John Deere fully recognizes the need to conduct business with integrity. Our broad approach to citizenship, coupled with market leadership, helps us improve the world while growing a business."

Deere believes in creating and distributing service in ways that respect the earth's limited resources while providing commitment to helping find policy solutions that benefit the environment. "We believe that effective policy to address global climate change must include development and support of renewable energy sources including agricultural, forestry, wind and bio-technologies, as well as processing and distribution improvements," says Jenkins.

With a passionate commitment to doing what is right and operating ethically, John Deere makes their conduct guidelines transparent to employees, customers, and suppliers. Acting out of principled, long-term self-interest, Deere contributes to the greater good by supporting the quality of life in their communities, protecting the environment and preserving precious resources. According to Jenkins, "We believe that exceptional performance will not be sustainable if it is at the expense of our values."

SOURCE: Ethisphere.com (August 28, 2007).

GLOBAL Perspectives

U.S. Ethical Practices: How They Compare Globally

As the number of multinational firms increases, companies and nations inevitably become more interdependent, and they must learn to cooperate for mutual benefit. However, because of cultural differences, increased interdependence also heightens the potential for conflicts, many of which involve marketing ethics. In fact, developing nations may have trouble imposing their marketing, environmental, and human rights regulations on large multinational firms. Some of the major ethical issues faced by international marketers are:

- *Traditional small-scale bribery:* payment of a small sum of money (for example, a "grease payment" or kickback), typically to a foreign official, in exchange for his or her violation of some official duty or responsibility in an effort to speed routine government actions
- *Large-scale bribery:* relatively large payment (for example, a political contribution) intended to allow a violation of the law or to influence policy directly or indirectly
- *Gifts, favors, and entertainment:* lavish gifts; opportunities for personal travel at the company's expense; gifts received after the completion of a transaction; expensive entertainment
- *Pricing:* unfair differential pricing; questionable invoicing (when the buyer requests a written invoice showing a price other than the actual price paid); pricing to force out local competition; dumping products at prices well below those in the home country; pricing practices that are illegal in the home country but legal in the host country (for example, price-fixing agreements)
- *Products and technology:* products and technology that are banned for use in the home country but permitted in the host country (such as products containing asbestos or DDT); products that appear unsuitable or inappropriate for use by the people in the host country
- *Tax evasion:* practices used specifically to evade taxes; transfer pricing (adjusting prices paid between affiliates and the parent company so as to affect the allocation of profits); "tax havens" (shifting profits to a low-tax jurisdiction); adjusted interest payments on intrafirm loans; questionable management and service fees charged between affiliates and the parent company
- *Illegal or immoral activities in the host country:* practices such as polluting the environment; maintaining unsafe working conditions; copying products or technology where protection of patents, trade names, or trademarks has not been enforced; short-weighting overseas shipments so as to charge a phantom weight
- *Questionable commissions to channel members:* unreasonably large commissions or fees paid to channel members, such as sales agents, middlemen, consultants, dealers, and importers
- *Cultural differences:* differences between cultures involving potential misunderstandings related to the traditional requirements of the exchange process (for example, transactions regarded as bribes by one culture but acceptable in another)—including gifts, monetary payments, favors, entertainment, and political contributions that are not considered part of normal business practices in one's own culture
- *Involvement in political affairs:* marketing activities related to politics, including the exertion of political influence by multinationals, marketing activities when either the home or the host country is at war, and illegal technology transfer

Rank the preceding practices from those that would be least difficult to avoid to those that would be most difficult to avoid. Should international marketers who cannot avoid these practices simply be forbidden to sell products in a particular country?

in those countries. The act has been criticized for putting U.S. businesses at a competitive disadvantage. Many contend that bribery is an unpleasant but necessary part of international business.

ETHICAL DILEMMAS RELATED TO DEVELOPING COUNTRIES

For companies, the benefits of seeking international growth are several. A company that cannot grow further in its domestic market may reap increased sales and economies of scale not only by exporting its product but also by producing it abroad. A company may also wish to diversify its political and economic risk by spreading its operations across several nations.

Expanding into developing countries offers multinational companies the benefits of low-cost labor and natural resources. But many multinational firms have

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In the face of the rising number of smokers in their country, the Malaysian government has banned the advertising of tobacco products. However, many firms in the tobacco industry skirt the law by sponsoring sports and entertainment events, such as this motorsport event, or by advertising their brands without referring to cigarettes.

been criticized for exploiting developing countries. Although the firms' business practices may be legal, many business ethicists argue that they are unethical. The problem is compounded by the intense competition among developing countries for industrial development. Ethical standards are often overlooked by governments hungry for jobs or tax revenues.

Take the tobacco industry, for instance. With tobacco sales decreasing and regulations stiffening in the United States and Western Europe, tobacco companies have come to believe that their future lies elsewhere: in China, Asia, Africa, Eastern Europe, and Russia. Despite the known health risks of their product, the large tobacco companies are pushing their way into markets that typically have few marketing or health-labeling controls. In Hungary, Marlboro cigarettes are sometimes handed out to young fans at pop concerts. In the last 10 years, cigarette advertising on Japanese television has soared from 40th to 2nd place in air time and value; it appears even during children's shows.

Interestingly, at a time when smoking is being discouraged in the United States, U.S. trade representatives are talking to developing countries like China and Thailand about lowering their tariffs on foreign cigarettes. Japan, Taiwan, and South Korea have already given in to the threats. Entering these developing countries, the tobacco companies and trade representatives insist, will help U.S. tobacco manufacturers make up for losses in their home market. Worldwide, tobacco causes nearly 5 million deaths per year. It is expected to rise to 10 million by 2020.[18] Is it ethical for tobacco executives to promote and export this product?

Environmental issues are another example. As U.S. environmental laws and regulations gain strength, many companies are moving their operations to developing countries, where it is often less expensive to operate. These countries generally enforce minimal or no clean-air and waste-disposal regulations. For example, an increasing number of U.S. companies have located manufacturing plants called *maquiladoras* in Mexico, along the U.S.-Mexican border. Many blame the *maquiladoras* for "not putting back into the border area what they have been taking out," referring to the region's inadequate sewers and water-treatment plants.

Because Mexico has been eager to attract foreign employers, *maquiladoras* pay little in taxes, which would normally go toward improving the country's infrastructure. Cuidad Juárez, a populous and polluted *maquiladora* city bordering El Paso, Texas, generates millions of gallons of sewage a day and has no sewage system at all.

REVIEW LEARNING OUTCOME

LO 3 Describe the role of ethics and ethical decisions in business.

MORALITY

Preconventional	Conventional	Postconventional
What's in it for me?	Everyone else is doing it!	Is this good in the long run?
Will I get caught?	When in Rome. . .	

ETHICAL CLIMATE

TOP-MANAGEMENT'S ETHICS

MAGNITUDE OF CONSEQUENCES

SOCIAL CONSENSUS

PROBABILITY OF HARM

LENGTH OF TIME BETWEEN DECISION AND IMPACT

NUMBER OF PEOPLE AFFECTED

ETHICAL TRAINING

LO4
Corporate Social Responsibility

corporate social responsibility Business's concern for society's welfare.

sustainability The idea that socially responsible companies will outperform their peers by focusing on the world's social problems and viewing them as opportunities to build profits and help the world at the same time.

stakeholder theory A theory that holds that social responsibility is paying attention to the interest of every affected stakeholder in every aspect of a firm's operation.

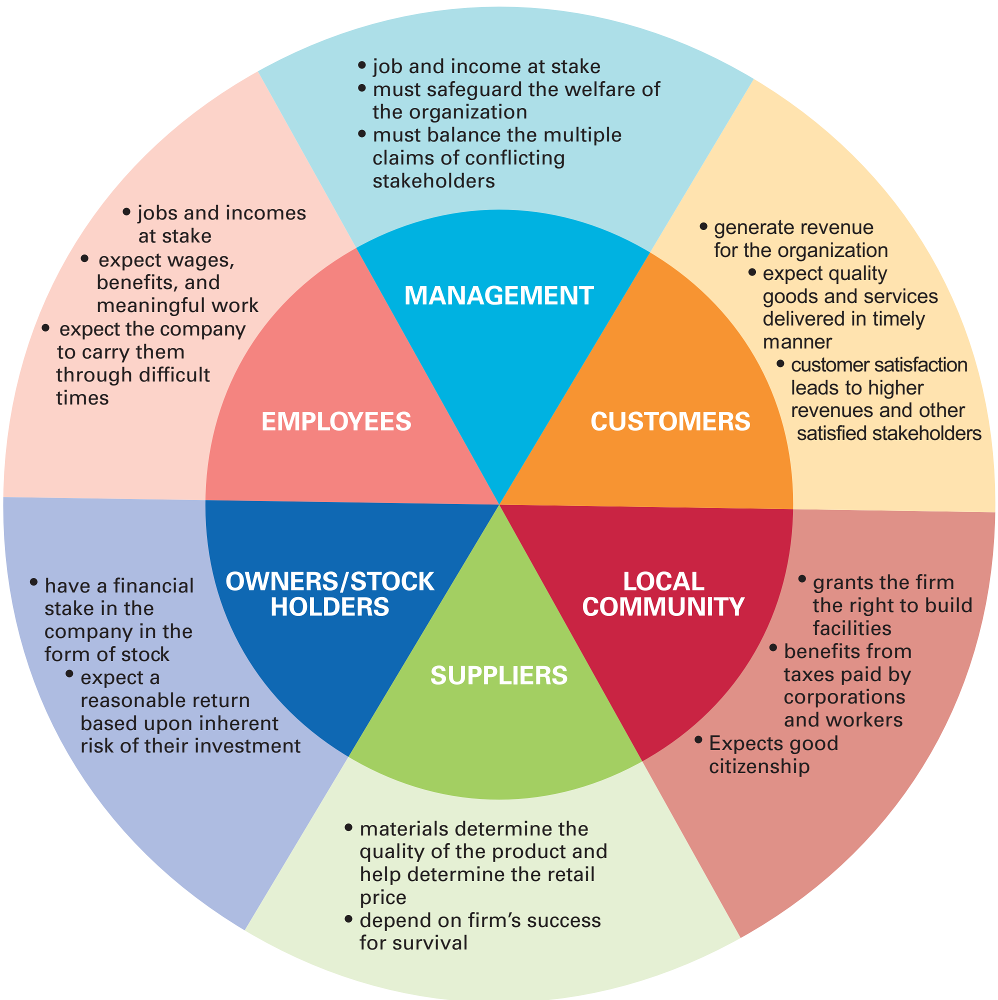
Corporate social responsibility is a business's concern for society's welfare. This concern is demonstrated by managers who consider both the long-range best interests of the company and the company's relationship to the society within which it operates. The newest theory in social responsibility is called sustainability. This refers to the idea that socially responsible companies will outperform their peers by focusing on the world's social problems and viewing them as opportunities to build profits and help the world at the same time. It is also the notion that companies cannot thrive for long (i.e., lack sustainability) in a world where billions of people are suffering and are desperately poor. Thus, it is in business's interest to find ways to attack society's ills. Only business organizations have the talent, creativity, and executive ability to do the job.

STAKEHOLDERS AND SOCIAL RESPONSIBILITY

A second approach to social responsibility is known as the stakeholder theory. This says that social responsibility is paying attention to the interest of every affected stakeholder in every aspect of a firm's operation.[19] The stakeholders in a typical corporation are shown in Exhibit 3.6.

Exhibit 3.6

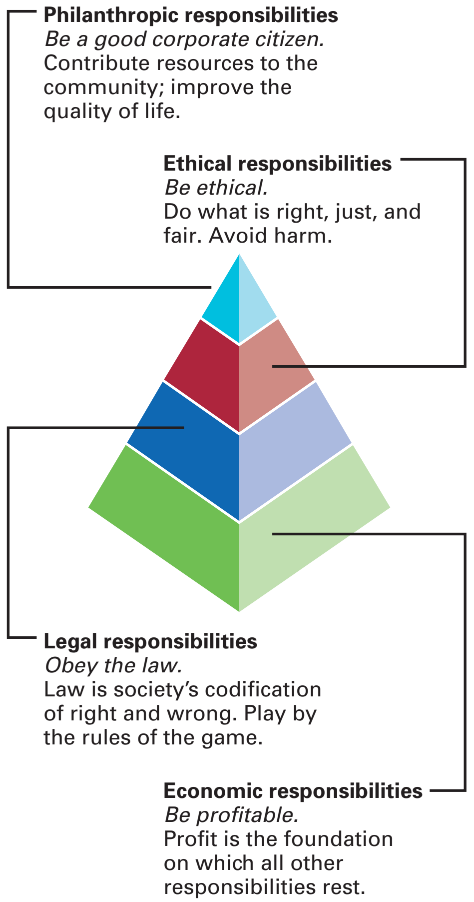
Stakeholders in a Typical Corporation



- *Employees* have their jobs and incomes at stake. If the firm moves or closes, employees often face a severe hardship. In return for their labor, employees expect wages, benefits, and meaningful work. In return for their loyalty, workers expect the company to carry them through difficult times.
- *Management* plays a special role, as they also have a stake in the corporation. Part of their stake is like that of the employees. On the other hand, management must safeguard the welfare of the organization. Sometimes this means balancing the multiple claims of conflicting stakeholders. For example, stockholders want higher return and perhaps lower costs by moving factories overseas. This naturally conflicts with employees, the local community, and perhaps suppliers.
- *Customers* generate the revenue for the organization. In exchange, they expect quality goods and services delivered in a timely manner. Customer satisfaction leads to higher revenues and the ability to enhance the satisfaction of other stakeholders.
- *The local community*, through its government, grants the firm the right to build facilities. In turn, it benefits directly from local taxes paid by the corporation and indirectly by property and sales taxes paid by the workers. The firm is expected to be a good citizen by paying a fair wage, not polluting the environment, and so forth.
- *Suppliers* are vital to the success of the firm. If a critical part, for example, is not available for an assembly line, then production grinds to a halt. The materials supplied determine the quality of the product produced and create a cost floor, which helps determine the retail price. In turn, the firm is the customer of the supplier and is therefore vital to the success and survival of the supplier. Small firms who sold most of their production to Wal-Mart and were subsequently dropped by Wal-Mart have sometimes gone bankrupt.
- *Owners* have a financial stake in the form of stock in a corporation. They expect a reasonable return based upon the amount of inherent risk on their investment. Often managers and employees have a portion of their retirement funds in company stock. In the case of Enron's bankruptcy, many workers lost their entire retirement savings.

REVIEW LEARNING OUTCOME

LO4 Discuss corporate social responsibility.



pyramid of corporate social responsibility
A model that suggests corporate social responsibility is composed of economic, legal, ethical, and philanthropic responsibilities and that the firm's economic performance supports the entire structure.

One theorist suggests that total corporate social responsibility has four components: economic, legal, ethical, and philanthropic. The **pyramid of corporate social responsibility** portrays economic performance as the foundation for the other three responsibilities. At the same time that it pursues profits (economic responsibility), however, a business is expected to obey the law (legal responsibility); to do what is right, just, and fair (ethical responsibilities); and to be a good corporate citizen (philanthropic responsibility). These four components are distinct but together constitute the whole. Still, if the company doesn't make a profit, then the other three responsibilities are moot.

LO 5

Arguments Against and For Corporate Social Responsibility

Today very few managers are against social responsibility initiatives. The debate, instead, is the degree and kinds of social responsibility that an organization should pursue.

ARGUMENTS AGAINST CORPORATE SOCIAL RESPONSIBILITY

Skeptics say business should focus on making a profit and leave social and environmental problems to nonprofit organizations (like the World Wildlife Federation or the Sierra Club) and government. Economist Milton Friedman believed that the free market, not companies, should decide what is best for the world. He asked, "If businesspeople do have a social responsibility other than making maximum profits for stockholders, how are they to know what it is?"[20] Friedman argued that when business executives spend more money than they need to—to purchase delivery vehicles with hybrid engines or to pay higher wages in developing countries, or even to donate company funds to charity—they are spending shareholders' money to further their own agendas. It is better to pay dividends and let the shareholders give the money away, if they choose.

Another argument is that businesses are created to produce goods and services, and not to handle welfare activities. They don't have the expertise to make social decisions. And if managers take time and monies to pursue social responsibilities, it will take away from the primary goals of the firm.

A final argument is that being socially responsible might damage the company in the global marketplace. That is, cleaning up the environment, ensuring product safety, and donating money and time for social causes all raise costs. This will be reflected in the final prices of the goods and services a company sells. In countries that don't emphasize social responsibility, a company will have lower costs because it doesn't engage in activities related to social responsibility. If the American company competes with the foreign competitor in the global marketplace, it will be at an economic disadvantage.

ARGUMENTS FOR SOCIAL RESPONSIBILITY

The most basic argument for social responsibility is that it is simply the right thing to do. Some societal problems have been brought about by corporations such as pollution and poverty-level wages; it is the responsibility of business to right these wrongs. Another position is that business has the resources, so business should be given the chance to solve social problems. For example, business can provide a fair work environment, safe products, and informative advertising.

Another, more pragmatic, reason for being socially responsible is that, if business isn't responsible, then government will create new regulations and perhaps levy fines against corporations. For example, Valero Energy was recently fined $4.25 million for pollution at three of its refineries and required to spend an additional $232 million on new pollution controls.[21] To the extent that business polices itself with self-disciplined standards and guidelines, government intervention can be avoided.

A final argument for social responsibility is that it can be a profitable undertaking. Smart companies, they say, can prosper and build shareholder value by tackling global problems. For General Electric, selling more wind power and energy-efficient locomotives is a no-brainer. When it comes to philanthropy, or supply chain audits designed to keep GE from being linked to sweatshops, or decisions about granting domestic-partner benefits, the business case usually comes down to GE's reputation and its desire to attract and engage great people. Some years back, for example, GE decided not to sell low-end ultrasound machines in China (and to put warning labels on the high-end machines it did sell) because it did not want the machines to be used for gender screening that could lead to abortions. The potential harm to GE's image was too great to take the risk.

But applying that kind of cost-benefit analysis to decisions with moral dimensions is a tricky business. Although GE operates in more than 100 countries, it has decided not to do business in Myanmar because the government there is a notorious violator of human rights and has been spotlighted by human-rights groups—and because the business upside is limited. GE has judged that it has more to lose than gain by being there.[22]

Wal-Mart has experienced its share of criticism for not paying a living wage, putting small independent firms out of business, and using too much energy. However, Wal-Mart has aggressively become pro-active toward the environment and hopes to make money by "being green." Lee Scott, Wal-Mart's CEO, vows to use 100 percent renewable energy, drastically reduce waste through recycling, and sell "sustainable" products that are more environmentally friendly. Cutting energy use is saving money, and consumers appreciate Wal-Mart's forays into organic cotton products and coffee certified to have earned farm workers a decent wage.

Switching stores to more efficient light bulbs and adding skylights for natural light has trimmed Wal-Mart's electricity bill by 17 percent since 2002. Using less packaging on house brand toys will save $2.4 million annually in shipping costs. Even Wal-Mart's push to slash America's electricity use—and thus greenhouse gas emissions—by selling 100 million compact fluorescent bulbs a year has a bottom-line benefit. Customers will save $3 billion and the expectation is that these savings will come back in terms of purchases at Wal-Mart.[23]

Some other companies that profit from being socially responsible are shown in Exhibit 3.7. One recent study found that, for large companies, a one percent increase in the firm's social responsibility ratings led to a $17 million increase in profits.[24]

GROWTH OF SOCIAL RESPONSIBILITY

Social responsibility of businesses is growing around the world. A recent study of social responsibility, in selected countries, asked the following: "Does your company consider social responsibility factors when making business decisions?" The percentage of firms that said "yes" were: Brazil, 62 percent; Canada, 54 percent; Australia, 52 percent; America, 47 percent; India, 38 percent; China, 35 percent; Mexico, 26 percent.[25]

Another survey pointed out that 47 percent of American firms was simply not adequate. Seventy-five percent felt that United States companies needed to do more in the area of social responsibility.[26]

Proactive Social Responsibility

Two companies that are frequently lauded for their social responsibility are food giant H. J. Heinz and Chiquita, the banana grower. Heinz has been a leader in social responsibility from its inception. For Chiquita, its awakening came later.

H. J. Heinz[27]

Founded in 1869, H. J. Heinz Co. was socially responsible long before corporate social responsibility became a banner corporations were advised to adopt. In fact, founder Henry Heinz was one of the first advocates of pure food and corporate transparency. "Our history is captured by the pure food products label," says Ted Smyth, SVP and chief administrative officer for Heinz. "Realizing horseradish was being sold with ingredients like sawdust to fill it out, Henry Heinz used a clear bottle so the consumer could see it wasn't adulterated. It was a great success and brilliant marketing."

Exhibit 3.7

Doing Well by Doing Good

Automobiles

Toyota: The maker of the top-selling Prius hybrid leads in developing efficient gas-electric vehicles.

Renault: Integrates sustainability throughout organization; has fuel-efficient cars and factories.

Volkswagen: A market leader in small cars and clean diesel technologies.

Computers & Peripherals

Hewlett-Packard: Despite board turmoil, the company rates high on ecological standards and digital technology for the poor.

Toshiba: At the forefront of developing eco-efficient products, such as fuel cells for notebook PC batteries.

Dell: Among the first U.S. PC makers to take hardware back from consumers and recycle it for free.

Retail

Marks & Spencer: Buys local product to cut transit costs and fuel use; good wages and benefits help retain staff.

Home Retail Group: High overall corporate responsibility standards have led to strong consumer and staff loyalty.

Aeon: Environmental accounting has saved $5.6 million; good employee policies in China and SE Asia.

Household Durables

Philips Electronics: Top innovator of energy-saving appliances, lighting, and medical gear and goods for the developing world.

Sony: Is ahead on green issues and ensuring quality, safety, and labor standards of global suppliers.

Matsushita Electric: State-of-the-art green products; eliminated 96 percent of the most toxic substances in its global operations.

Pharmaceuticals

Roche: Committed to improving access to medicine in poor nations; invests in drug research for Third World.

Novo Nordisk: Spearheads efforts in diseases like leprosy and bird flu and is a leading player in lower-cost generics.

Glaxo-SmithKline: One of few pharmas to devote R&D to malaria and TB; first to offer AIDS drugs at cost.

Utilities

FPL: Largest U.S. solar generator; has 40 percent of wind-power capacity; strong shareholder relations.

SOURCE: "Who's Doing Well by Doing Good," *Business Week*, January 29, 2007, 53. Reprinted from the January 29, 2007 issue of 'Business Week' by special permission, copyright © 2007 by The McGraw-Hill Companies, Inc.

These days, consumers are concerned with not only the quality, but also the nutritional content of foods. More than 70 percent of Heinz products can be classified in the health category, and incremental health improvements are planned. Ingredients such as trans fat, salt, and sugar are being removed. Organic varieties are available, and many foods are being fortified with vitamins and minerals. "We operate in fundamentally healthy categories," says Andrew Towle, VP of global marketing. "Removing ingredients of concern is a technical challenge. We cannot go backward in taste."

Established in 1951, The Heinz Co. Foundation (HCF) is funded by the company to promote health, nutrition, and well-being in communities where Heinz operates. Indeed, social responsibility is undeniably part of Heinz's DNA, yet many are unaware of it because social responsibility is standard practice. In 2002, HCF began its micronutrient program, supported by Dr. Stanley Zlotkin, creator of Sprinkles, an iron-supplement multivitamin powder. The company has used existing packaging and distribution channels to deliver the supplements to more than 1.2 million children in 15 countries. "Sixty packets can cure one child of anemia for a year," says HCF director Tammy Aupperle. "We hope to reach 10 million by 2010." In 2003, Heinz and Helen Keller International, which fights causes and consequences of blindness and malnutrition, partnered in Indonesia. They distributed more than

44 million supplement packets, benefiting more than 400,000 people. The model will be replicated in India and China.

A few additional Heinz initiatives are:

- *Nutrient program:* Nutritional supplement packets have been distributed to more than 1.2 million children in Indonesia, Guyana, Mongolia, Pakistan, Haiti, Ghana, and other countries.
- *Health and wellness initiatives:* A Global Health & Wellness Task Force is addressing ingredients of concern (sodium, sugar, and others), adding more goodness to products, and adding functional benefits for consumers.
- *Sustainable agriculture:* Agricultural practices include hybrid seeds, water conservation and reuse, recycling waste, minimal pesticide use, and partnership with Chinese government and farmers.
- *Eco-friendly packaging:* New packaging includes reduced steel, recycled paper trays and cartons, non-bleached cartons, and reduced resin use.

Heinz is a firm that truly cares about its stakeholders.

Chiquita Cleans Up Its Act[28]

"For decades the $3.9-billion-a-year fruit giant was synonymous with the notion of the greedy multinational. Farmworkers toiled long hours in dangerous conditions, agrochemical runoff contaminated water, and tropical forests were cleared for expansion," says J. Gary Taylor, coauthor of *Smart Alliance*, a book about Chiquita.

Enter Rainforest Alliance, which had previously worked with timber companies in Indonesia to lessen the impact of logging. In 1992 the Alliance sent banana companies a list of environmental and worker-rights standards required to gain its certification. During the next two years, Dave McLaughlin, Chiquita CEO, says Chiquita spent 400,000 to overhaul the Costa Rican farms, phase out toxic pesticides, and build new warehouses to store chemicals. McLaughlin began monitoring water quality and providing workers with better safety equipment. The farms also started recycling programs.

Today all 110 of Chiquita's company-owned farms and the vast majority of its independent farms are certified by the Rainforest Alliance. Things are getting better for its Latin American employees, who can now join unions. Four recent initiatives are:

- One hundred percent of the plastic bags and twine used on Chiquita farms is recycled.
- Pesticide use has been cut by 26 percent, and workers are provided with better protective gear.
- Working conditions have been improved by new Chiquita-built housing and schools for employees' families.
- Buffer zones along farm borders help prevent chemical runoff and erosion.

REVIEW LEARNING OUTCOME

LO5 Describe the arguments for and against social responsibility.

FOR	AGAINST
On the one hand:	**On the other hand:**
• it's the right thing to do • government will create new regulations and levy fines if firms aren't socially responsible • it can enhance a company's profitability	• the job of the corporation is to maximize profits for stockholders • businesses are better suited to produce goods and services and not to be involved in welfare services • if global competitors don't have to be socially responsible, they will have lower costs and can compete more effectively in the global marketplace


THE COST OF IGNORING SOCIAL RESPONSIBILITIES[29]

In today's environment, a firm that disregards its stakeholders and its social responsibilities does so at its own peril. In the case of AOL, it didn't treat its customers (key stakeholders) as they should have been treated. A deluge of AOL customers complained that they tried to close their accounts only to be thwarted in their attempts or to discover they were still being billed for services that they thought had been canceled. Although it had long been one of the Internet's best-known companies, AOL didn't set up an online cancellation system. All cancellation requests had to be made by fax, mail or telephone. Subscribers who phoned AOL to cancel their service sometimes were greeted by aggressive customer service representatives who were paid bonuses of up to $3,000 if they found a way to retain the business. Customers complained that AOL's incentive system created an obstructive culture that made service cancellations difficult. "Consumers who called were put on hold or transferred repeatedly until they hung up in disgust," says Connecticut Attorney General Richard Blumenthal, who described AOL's practices as "outlandish and underhanded."

These customer complaints led to a $3 million settlement with 48 states and the District of Columbia. As part of the resolution, AOL agreed to make it easier for its remaining customers to leave and to maintain an online channel for processing cancellations.

LO 6

Cause-Related Marketing

cause-related marketing The cooperative marketing efforts between a "for-profit" firm and a "nonprofit organization."

A sometimes controversial subset of social responsibility is cause-related marketing. Sometimes referred to as simply "cause marketing," it is the cooperative efforts of a "for-profit" firm and a "nonprofit organization" for mutual benefit. Cause-related marketing is sometimes used as any marketing effort for social or other charitable causes. Cause marketing differs from corporate giving (philanthropy) as the latter generally involves a specific donation that is tax deductible, while cause marketing is a marketing relationship not based on a straight donation.

Cause-related marketing is very popular and is estimated to generate about $7 billion a year in revenue.[30] It creates good public relations for the firm and will often stimulate sales of the brand. Yet, the huge growth of cause-related marketing can lead to a case of consumer cause fatigue. A 2007 nationwide survey found that 36 percent said they bought a product in the previous 12 months after learning of its maker's commitment to social issues, down from 43 percent in 2004. Only 14 percent said they intentionally paid more for a product that supports a cause, down from 28 percent. And just 30 percent said they told a family member or friend about a product or company committed to a social issue, compared with 43 percent in 2004.[31]

Examples of cause-related marketing abound. Starwood Hotels has announced that for every Westin Heavenly Bed, Sheraton Sweet Sleeper Bed, and Four Points by Sheraton Four Comfort Bed sold through Starwood retail channels, the firm will donate $50 to the special Olympics. Avaya recently publicized that it will donate $5 to the American Cancer Society for each pink desk phone faceplate it sells. The money is to be used to raise breast cancer awareness. Starbucks donates 5 cents of every sale of Ethos Water to help children around the world get access to clean drinking water. American Express launched a campaign to restore the Statue of Liberty and Ellis Island. The company contributes 1 cent per card transaction and $1 for every new card issued. American Express collected $1.7 million for the restoration effort.[32]

CAUSE-RELATED MARKETING CONTROVERSY

Few causes have been more saturated with marketing than breast cancer awareness. Consumers can buy everything from food to toilet paper with labels that feature a pink ribbon. This generally signifies that for each product sold money is donated to breast cancer awareness. Yoplait ran a campaign that donated 10 cents to the Canadian Breast Cancer Foundation every time a consumer mailed back one of its yogurt carton lids. Aside from the fact that someone would have to eat three cartons of yogurt a day for more than three months just to raise $20, and that consumers spent more on postage than they raised with each lid, Yoplait left it to the fine print to state it was capping donations at $80,000—keeping the rest as profit.[33]

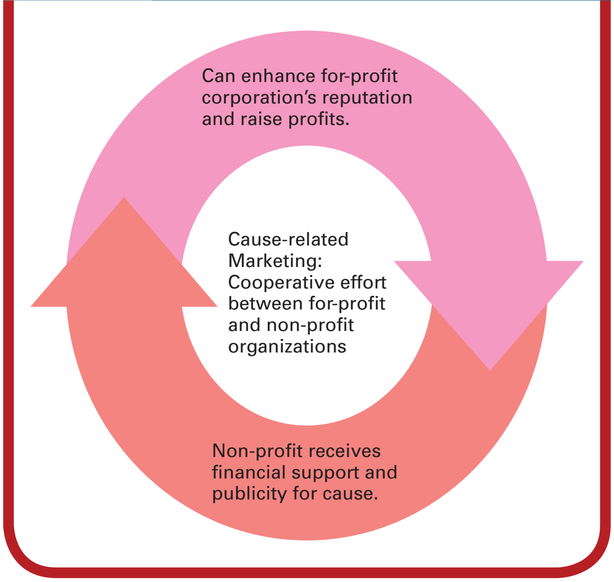
The Gap has been criticized for The Gap (Product) Red campaign. Thanks to the Gap and others, more than $25 million has been raised to fight HIV/AIDS, tuberculosis, and malaria. The Gap has stated that "50 percent of (Product) Red products" are being directed to the cause. Yet the promotional expenditures for the (Product) Red campaign were $100 million![34]

The Susan G. Komen Breast Cancer Foundation is on the receiving end of much cause-related marketing. The Foundation recently put out an information piece entitled, "Five Questions to Ask Before Participating in a Cause-Related Marketing Program." The questions are:

1. Is this company committed? Read the product packaging and promotional materials or display and visit the company Web site to make sure the company is credible and committed to the cause.
2. How is the program structured? Transparency is key. Is the company clearly stating how the money is raised and how much will be going to charity? For example, if it's a donation per purchase, ask how much of purchase price goes to charity—is it two percent or 10 percent—or some other amount? If there is a minimum contribution guaranteed by the company, what is the amount? Is there a maximum donation that will be made by the company?
3. Who does the program benefit? Does it support a well-managed, reputable non-profit or fund? Again, we recommend that consumers read Web sites. The Komen Foundation makes it very clear on our site who we are, how we structure programs and how the monies are used. The Better Business Bureau Wise Giving Alliance is one resource for information on non-profit organizations.
4. How will the organization that benefits use my money? It should be abundantly clear where the monies go. What organization will they support? Will the dollars generated go to research, education, community programs or all of the above? The Komen Foundation is very specific about our programs, activities and grants awarded to support our mission to eradicate breast cancer as a life-threatening disease. Visit **http://www.komen.org** to view the Komen Foundation's most recent Annual Report.
5. Is the program meaningful to me? Is the program supporting a cause you believe in or have been touched by? Based on the details of the program and the potential for dollars to be raised, does the program make sense to you? Selecting the right program is a personal choice based on your interests, your passions and a cause that is important to you.[35]

REVIEW LEARNING OUTCOME

LO 6 Explain cause-related marketing.



13 < percent of today's large-company top executives who report that having strong ethical traits is the most important leadership trait of CEOs

20 < percent of large-company top executives in 2003 who reported that having strong ethical traits was the most important leadership trait of CEOs

37 < percent of large-company top executives who report that the most important trait of CEOs is the ability to inspire others

percent of companies surveyed had a code of ethics > **60**

33 < percent of companies surveyed offered ethics training

percent of companies surveyed employed an ethics officer > **33**

Review and Applications

LO 1 Explain the determinants of a civil society. The "social glue" that holds a society together is comprised of six factors. They are ethics, laws, formal and informal groups, self-regulation, the media, and an active civil society. All of these are necessary for a coherent, vibrant, and civil society. These six factors are more important in countries than ever before because of the increasing complexity of the global economy and the melding of customs and traditions within societies.

1.1 Explain how each of the six factors contributes to a civil society.

1.2 Why is a free and uncontrolled media important in a country?

1.3 Can customs and laws sometimes conflict, especially when a society experiences an influx of immigrants?

LO 2 Explain the concept of ethical behavior. Ethics are the moral principles or values that generally govern the conduct of an individual or a group. Ethics can also be viewed as the standard of behavior by which conduct is judged. Ethical conflicts sometimes arise between business owners, managers, customers, workers, and the surrounding community. Conflicts can sometimes be resolved through the reliance on ethical theories. Ethical theories that are applicable to marketing include deontology, utilitarianism, casuist, moral relativism, and virtue ethics.

2.1 It is sometimes said that ethics hold a person to higher standards than laws. Explain.

2.2 Moral relativists are basically time and place ethicists. Explain what this means.

2.3 Explain the differences between utilitarianism, casuist, and deontology theories.

LO 3 Describe ethical behavior in business. The law typically relies on juries to determine whether an act is legal or illegal. Society determines whether an action is ethical or unethical. Morals are the rules that people develop as a result of cultural values and norms. More and more companies are using ethics training to help put good ethics into practice. Ethical beliefs vary a little from culture to culture. However, some ethical practices vary significantly from one culture to the next.

3.1 Explain the difference between ethics and morals and describe the relationship between the two.

3.2 What are the differences between preconventional morality, conventional morality, and postconventional morality? Give an example of each.

3.3 Give several examples of how ethical practices can vary from one culture to the next.

LO 4 Discuss corporate social responsibility. Responsibility in business refers to a firm's concern for the way its decisions affect society. A second theory says that the corporation should always pay attention to the interests of its stakeholders. These are management, customers, the local community, owners/stockholders, suppliers, and employees. Social responsibility has four components: economic, legal, ethical, and philanthropic. These are intertwined, yet the most fundamental is earning a profit. If a firm does not earn a profit, the other three responsibilities are moot. Most business-people believe they should do more than pursue profits. Although a company must consider its economic needs first, it must also operate within the law, do what is ethical and fair, and be a good corporate citizen. The concept of sustainability is that socially responsible companies will outperform their peers by focusing on the world's social problems and viewing them as an opportunity to earn profits and help the world at the same time.

4.1 Describe at least three situations in which you would not purchase the products of a firm even though it is very socially responsible.

4.2 A firm's only responsibility to society is to earn a fair profit. Comment.

4.3 Is sustainability a viable concept for America's businesses?

4.4 Illustrate how there can be conflicts between the needs and desires of various stakeholders.

LO 5 Describe the arguments for and against social responsibility. Today, virtually all managers endorse social responsibility of corporations. It is, instead, a matter of what types of responsibility and the degree of responsibility. The arguments against social responsibility are: The job of the corporation is to maximize profits for stockholders; Businesses are better suited to produce goods and services and not to be involved in welfare services; If global competitors aren't socially responsible they will have lower costs and can compete more effectively in the global marketplace. The arguments for social responsibility are: It's the right thing to do; Government will create new regulations and levy fines if firms aren't socially responsible; Social responsibility can enhance a company's profitability.

5.1 Explain the relationship between the global economy and social responsibility.

5.2 Defend the proposition that the only responsibility of the firm is to make money for the stockholders.

5.3 Explain how a firm can earn additional profits by being socially responsible.

LO 6

Explain cause-related marketing. Cause-related marketing is the cooperative effort between a for-profit firm and a non-profit organization. It is different from philanthropy, which is a specific, tax deductible donation. Cause-related marketing is very popular because it can enhance the reputation of the corporation and also make additional profit for the company. Sometimes companies have abused cause-related marketing and received much greater benefits than the nonprofit that has supposedly been helped. These cases are a small minority.

6.1 Why are more firms jumping on the cause-related marketing bandwagon?

6.2 Explain the controversy surrounding some cause-related marketing.

6.3 What are some questions that consumers should consider before participating in a cause-related campaign?

Key Terms

casuist ethical theory	65	ethics	63	pyramid of corporate social responsibility	76
cause-related marketing	81	Foreign Corrupt Practices Act	71	stakeholder theory	75
code of ethics	69	utilitarian ethical theory	64	sustainability	75
corporate social responsibility	75	morals	67	virtue	65
deontological ethical theory	64	moral relativists	65		

Exercises

APPLICATION EXERCISE[36]

Many companies today are concerned with social responsibility. They may pursue philanthropic activities and/or strive to be ethical. Your goal for this assignment is to evaluate how firms are being socially responsible. Limit your answers to one page and provide a printout of the Web site you visited.

Activities

ONLINE

1. Choose a company and find that company's Web site on the Internet. Once you get to the Web site, look for information that tells you about the firm's efforts to be socially responsible. Look for things like news releases, company information, information about community programs, etc. Look in your textbook and your notes to help you define what might be considered socially responsible activities. Describe what you find and explain why you think the company is involved with the activities you describe.
2. Do the activities described on the Web site seem consistent with the company's products? Why or why not? (For example, a shoe company may sponsor a race that raises money to help prevent a disease. People who participate in the race may use that company's running shoes and therefore the race would be consistent with the company's products.)
3. Evaluate how effective you think the information you find is in terms of how it is presented, what impact it might have and whether it will help to sell the company's products. Be sure to support any claims you make.

4. Does the information you collected during this activity improve your evaluation of the company? Would it influence your decision to buy the company's product? Why or why not?

ETHICS EXERCISE

Jane Barksdale has designed a line of clothing targeted toward Hispanic Americans. The items are sold only by catalog and on the Internet. She thinks that she can increase sales by claiming in ads that the firm is owned by a Hispanic American and all the employees are Hispanic Americans. She is not Hispanic American nor are most of the employees. She needs a high level of sales to pay her bank loan and remain in business.

Questions

1. Should Jane claim that she is Hispanic American? Explain your response.
2. Does the Federal Trade Commission address this issue? Go to http://www.ftc.gov and search for guidelines for small business advertising or e-commerce. What does Jane risk in making false claims in her ads?

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Case Study: Product (Red)

CAN A T-SHIRT SAVE THE WORLD?[37]

When Oprah and Bono walked down Chicago's Magnificent Mile together in the fall of 2006, it was the shopping trip seen around the world. The famous duo attracted mobs of fans and extensive media coverage as they promoted a revolutionary new cause-marketing event called (Product) RED. Bono urged people to buy RED products, explaining that a portion of the proceeds would go to The Global Fund to fight HIV/AIDS in Africa. Oprah, wearing an "INSPI(RED)" Gap t-shirt on her talk show that day, proclaimed, "I am wearing the most important t-shirt I've ever worn in my life!"

Other companies that licensed the RED brand and created products for the charity included Apple, which sold a limited edition iPod nano, and Motorola, which introduced a red Motorazr phone. Emporio Armani designed a special RED capsule collection for London Fashion Week, and Converse designed a line of RED shoes to be sold at Gap stores.

Oprah's shopping spree with Bono drew a reported an incredible one billion media impressions worldwide. (Product) RED set up its own Web site, **www.joinred.com**, and took over Myspace.com for the day to launch a page that now boasts over 600,000 friends. RSS (Really Simple Syndication) funneled news about RED to mobile phones and blog sites, and it quickly became a hot topic of discussion on message boards across the Internet.

(Product) RED was the brainchild of Bono and Bobby Shriver, who designed it as a commercial initiative that could change the way causes are marketed in the future. "They didn't want a one-time event," says Julia Cordua, VP of marketing. "They want five to ten years of ongoing donations."

Gap initially offered to give 100 percent of its profits on red products to the cause, but Bono and Shriver refused to accept more than 50 percent. Shriver insists that they want companies to make money off the campaign, explaining, "We want people buying houses in the Hamptons based on this because if that happens, this thing is sustainable." As a result, Gap treats RED like a business, spending millions on marketing it. Within months of its launch, they saw sales of an estimated $71 million in revenue and donated about $2.5 million to The Global Fund.

According to the (Product) RED Web site, "Each company that becomes (RED) places its logo in this embrace and is then elevated to the power of red." You can be embraced by the RED, it suggests, by purchasing a Gap T-shirt or African-print Converse shoes. "What better way to become a good-looking Samaritan?!"

Some critics, such as Charles Kernaghan, Director of the National Labor Committee for Worker and Human Rights, aren't buying it, though. "The thought of using consumer dollars made off the backs of workers held in sweatshops to help fund Bono's causes is really hypocritical—that's not the way to go," he says, referring to Gap's reputation for using factories that violate labor laws.

Since 2004 Gap has been working to combat this type of criticism by releasing Social Responsibility Reports on Gap factories in over 50 countries. Despite their efforts, however, nearly half of the factories still failed inspection as recently as 2005. When questioned, a Gap spokesperson responded by stating that Bono himself had inspected the African factory where RED products were being made, and it was "sparkling."

Some bloggers remain skeptical of the fundraiser, however, declaring it "khaki colonialism." Michael Medved argued that it would be better to forget the over-priced T-shirts and send money directly to The Global Fund. But whether you agree with the way (Product) RED does business or not, the campaign is hard to ignore. David Hessekiel of the Cause Marketing Forum proclaimed it "the launch of the year." Stacy Palmer of *The Chronicle of Philanthropy*, wrote, "These are iconic brands that appeal to younger consumers who are very interested in buying cause-related products. (Product) RED borrows on ideas that have been used a lot, but its scale makes it different. People are getting bombarded by RED."

(Product) RED president Tamsin Smith reported on the campaign's blog that much of the merchandise was sold out within hours of the launch. Oprah's INSPI(RED) t-shirt went on to become the bestselling item in the Gap's 35-year history. Long-term success, however, depends on how well the participating brands continue to market new products. They'll have to find ways to keep socially conscious consumers interested in RED now that most of them have been there, done that, and (literally) bought the T-shirt.

Questions

1. Discuss the four components of corporate social responsibility (CSR) and how they relate to a charitable campaign such as (Product) RED. How does participation in a cause-marketing event contribute to a company's CSR? What role does sustainability play?
2. Do you think a partnership with (Product) RED can improve Gap's image? Is it a sign that they are making a commitment to corporate social responsibility or do you agree with critics who say their involvement is an attempt to spit-shine the company's image while continuing to do business as usual?
3. Describe the various types of technology that have contributed to the media coverage, marketing efforts, and public discussion of the RED campaign.
4. A year after (Product) RED's launch, *Ad Age* reported that although $100 million had been spent on marketing the campaign, only about $25 million had gone to the charity itself. Industry observers speculated that this could trigger a backlash against the campaign. Do you believe the criticism is justified? Do you think the campaign could lose supporters as a result?

Company Clips

METHOD – PEOPLE AGAINST DIRTY

method's first "lab" was the kitchen of founders Eric Ryan and Adam Lowry, two friends whose goal was to evolve the household cleaner from a toxic object that hid under the sink to an all-natural, biodegradable, and stylish counter-top accessory. This video segment shows method through yet another lens, that of corporate social responsibility (CSR) and sustainability. Chemical engineer Adam Lowry outlines the chemical aspects of traditional cleaning products and describes how method's products are healthier. As you watch the video, keep in mind the various marketing orientations you learned in Chapter 1.

Questions

1. Does method have a societal marketing orientation, or is it just a market-oriented company that integrates a number of environmental practices into its operations? Explain.
2. How is method practicing sustainability?
3. Discuss the changing social factors that have made it possible for method to be so successful.

Marketing & You Results

The higher your score, the more important you think ethics and socially responsible behavior are to achieving corporate objectives. A high score also suggests that you are an ethical idealist, or someone who sees right and wrong as absolute, rather than an ethical relativist, or someone who sees right and wrong as situation dependent.

The Marketing Environment

CHAPTER

4

Learning Outcomes

LO 1 Discuss the external environment of marketing, and explain how it affects a firm

LO 2 Describe the social factors that affect marketing

LO 3 Explain the importance to marketing managers of current demographic trends

LO 4 Explain the importance to marketing managers of multiculturalism and growing ethnic markets

LO 5 Identify consumer and marketer reactions to the state of the economy

LO 6 Identify the impact of technology on a firm

LO 7 Discuss the political and legal environment of marketing

LO 8 Explain the basics of foreign and domestic competition

LO 1

The External Marketing Environment

If there is one constant in the external environment (outside the firm) where firms work and compete, it is that things are constantly changing. If the organization doesn't understand or fails to react to the changing world around it, it will soon be a follower rather than a leader. In the worst case scenario, the firm disappears from the marketplace. Applebee's was, at one time, a hot, trendy restaurant chain. Now, the company faces falling profits and unhappy stockholders. What happened? Applebee's didn't adapt quickly enough to the changing environment. High gasoline prices resulted in many customers staying at home. More importantly, it didn't change quickly enough when competitors copied it. Newer eateries offer slick interiors in contrast with Applebee's busy walls full of photos and sports memorabilia. Menus at many newer generation restaurants stress the freshness or naturalness of the food. Applebee's still focused on the fried and breaded items.[1]

Perhaps the most important decisions a marketing manager must make relate to the creation of the marketing mix. Recall from Chapters 1 and 2 that a marketing mix is the unique combination of product, place (distribution), promotion, and price strategies. The marketing mix is, of course, under the firm's control and is designed to appeal to a specific group of potential buyers. A target market is a defined group that managers feel is most likely to buy a firm's product.

target market
A defined group most likely to buy a firm's product.

As the Applebee's example shows, managers must alter the marketing mix because of changes in the environment in which consumers live, work, and make purchasing decisions. Also, as markets mature, some new consumers become part of the target market; others drop out. Those who remain may have different tastes, needs, incomes, lifestyles, and buying habits than the original target consumers.

Although managers can control the marketing mix, they cannot control elements in the external environment that continually mold and reshape the target market. Review Learning Outcome 1 shows the controllable and uncontrollable variables that affect the target market, whether it consists of consumers or business purchasers. The uncontrollable elements in the center of the diagram continually evolve and create changes in the target market. In contrast, managers can shape and reshape the marketing mix, depicted on the left side of the diagram, to influence the target market. That is, managers react to changes in the external environment and attempt to create a more effective marketing mix.

Marketing & You

Using the following scale, enter the numbers that reflect your opinions.

1	2	3	4	5	6	7
Strongly disagree						Strongly agree

— I need more hours in the day to get my work done.

— I *don't* have to overextend myself to find the time to get my work done.

— I feel as if I'm always "fighting fires."

— I seldom have to take shortcuts to get my work done on time.

— I never have enough time to think ahead.

— I feel as if I have a lot of time on my hands.

— I feel as if no matter how hard I work, I'll never get caught up.

Total your score. Read the chapter and find out what your score means at the end.

SOURCE: From Scale #119, Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds. Vol. III © by American Marketing Association.

UNDERSTANDING THE EXTERNAL ENVIRONMENT

Unless marketing managers understand the external environment, the firm cannot intelligently plan for the future. Thus, many organizations

Philips Electronics is a firm that is proactive in trying to keep a step ahead of the latest environmental trends. The firm's new strategic plan focuses on "sense and simplicity."

assemble a team of specialists to continually collect and evaluate environmental information, a process called *environmental scanning*. The goal in gathering the environmental data is to identify future market opportunities and threats.

Philips Electronics is a firm that is proactive in trying to keep a step ahead of the latest environmental trends. The firm's new strategic plan focuses on "sense and simplicity." The idea is to give consumers what they want in the way of electronic products in the health, lifestyle, and technology areas. Because Philips is dominated by engineers, it decided that if it was really going to create products that are simple to use and consumer-oriented, it needed help. The company created a four-person advisory group of opinion leaders from around the globe. The group consists of Sara Berman, a British fashion designer; Dr. Peggy Fritzsche, a California radiology professor; Gary Chang, a leading Chinese architect; and John Maeda, an MIT graphic designer. They meet several days each month in places like Paris, Rome, or New York to help Philips understand how the environment of business is changing. Their goal is to help Philips create intuitive, easy-to-use products that meet specific needs. Andrea Ragnatti, Chief Marketing Officer for Philips, notes that it took the firm quite a while to adopt the marketing concept. She notes, "In the past we just developed the technology and hoped someone would buy it. Now we are starting from the point of discovering what exactly consumers want a product to do."[2]

ENVIRONMENTAL MANAGEMENT

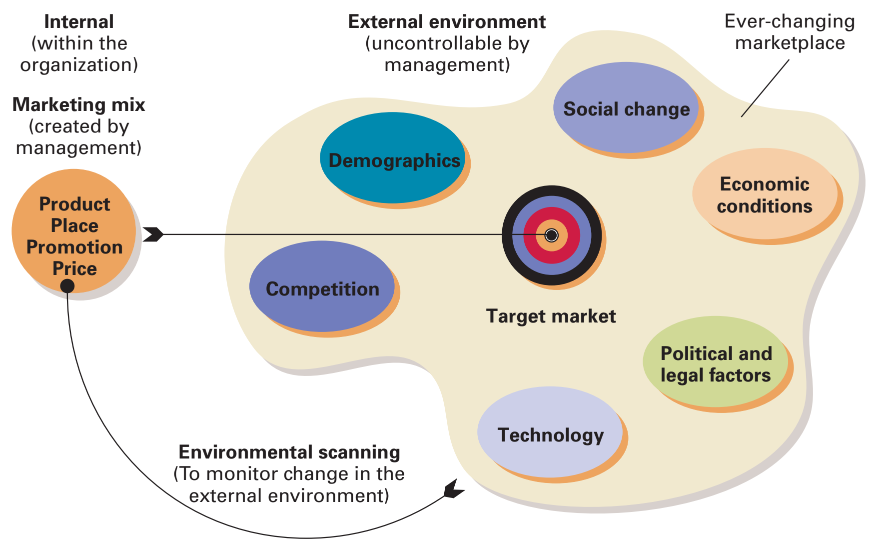
No one business is large or powerful enough to create major change in the external environment. Thus, marketing managers are basically adapters rather than agents of change. For example, despite the huge size of General Motors and Ford, these companies are continually challenged to meet the competitive push by the Japanese for an ever-growing share of the U.S. automobile market. Toyota is now America's most popular brand of automobile. Competition is basically an uncontrollable element in the external environment.

A firm is not always completely at the mercy of the external environment, however. Sometimes a firm can influence external events. For example, extensive lobbying by FedEx has enabled it to acquire virtually all of the Japanese routes that it has sought. Japan had originally opposed new cargo routes for FedEx. The favorable decision was based on months of lobbying by FedEx at the White House,

REVIEW LEARNING OUTCOME

LO 1 Discuss the external environment of marketing, and explain how it affects a firm

Uncontrollable Elements in the External Environment Create Opportunities and Threats for a Firm's Marketing Mix



at several agencies, and in Congress for help in overcoming Japanese resistance. When a company implements strategies that attempt to shape the external environment within which it operates, it is engaging in environmental management.

The factors within the external environment that are important to marketing managers can be classified as social, demographic, economic, technological, political and legal, and competitive.

LO 2 Social Factors

Social change is perhaps the most difficult external variable for marketing managers to forecast, influence, or integrate into marketing plans. Social factors include our attitudes, values, and lifestyles. Social factors influence the products people buy, the prices paid for products, the effectiveness of specific promotions, and how, where, and when people expect to purchase products.

AMERICAN VALUES

environmental management When a company implements strategies that attempt to shape the external environment within which it operates.

component lifestyles The practice of choosing goods and services that meet one's diverse needs and interests rather than conforming to a single, traditional lifestyle.

A *value* is a strongly held and enduring belief. During the United States' first 200 years, four basic values strongly influenced attitudes and lifestyles:

- *Self-sufficiency*: Every person should stand on his or her own two feet.
- *Upward mobility*: Success would come to anyone who got an education, worked hard, and played by the rules.
- *Work ethic*: Hard work, dedication to family, and frugality were moral and right.
- *Conformity*: No one should expect to be treated differently from everybody else.

These core values still hold for a majority of Americans today. A person's values are key determinants of what is important and not important, what actions to take or not to take, and how one behaves in social situations.

People typically form values through interaction with family, friends, and other influencers such as teachers, religious leaders, and politicians. The changing environment can also play a key role in shaping one's values. For example, people born during the 1980s and 1990s tend to be more comfortable with technology and its importance in the home than persons born in the 1960s.

Values influence our buying habits. Today's consumers are demanding, inquisitive, and discriminating. No longer willing to tolerate products that break down, they are insisting on high-quality goods that save time, energy, and often calories. U.S. consumers rank the characteristics of product quality as (1) reliability, (2) durability, (3) easy maintenance, (4) ease of use, (5) a trusted brand name, and (6) a low price. Shoppers are also concerned about nutrition and want to know what's in their food, and many have environmental concerns.

THE GROWTH OF COMPONENT LIFESTYLES

People in the United States today are piecing together component lifestyles. A lifestyle is a mode of living; it is the way people decide to live their lives. In other words, they are choosing products and services that meet diverse needs and interests rather than conforming to traditional stereotypes.

In the past, a person's profession—for instance, banker—defined his or her lifestyle. Today, a person can be a banker and also a gourmet, fitness enthusiast, dedicated single parent, and Internet guru. Each of these lifestyles is associated with different goods and services and represents a target audience. For example, for the gourmet, marketers offer cooking utensils, wines, and exotic foods through magazines such as *Bon Appetit* and *Gourmet*. The fitness enthusiast buys Adidas equipment and special jogging outfits and reads *Runner* magazine. Component lifestyles increase the complexity of consumers' buying habits. The banker may own a BMW but change the oil himself or herself. He or she may buy fast food for lunch but French wine for dinner, own sophisticated photographic equipment and a low-priced home stereo, and shop for socks at Kmart or Wal-Mart and suits or dresses at Brooks Brothers. The unique lifestyles of every consumer can require a different marketing mix.

THE CHANGING ROLE OF FAMILIES AND WORKING WOMEN

Component lifestyles have evolved because consumers can choose from a growing number of goods and services, and most have the money to exercise more options. The growth of dual-income families has resulted in increased purchasing power. Approximately 63 percent of all females between 16 and 65 years old are now in the workforce. Today, more than 10 million women-owned businesses in the United States, employing 18.2 million persons, generate $3.6 trillion in revenues.[3] The phenomenon of working women has probably had a greater effect on marketing than any other social change.

As women's earnings grow, so do their levels of expertise, experience, and authority. Working-age women are not the same group businesses targeted 30 years ago. They expect different things in life—from their jobs, from their spouses, and from the products and services they buy. Not all companies understand this notion. Even though women spend about $55 billion of the total $95 billion spent on consumer electronics, experts say companies continue to assume women aren't very interested in high-tech products or respond only to "technology-made-simple" themes.[4]

One industry that does seem to understand the importance of women buyers is the automobile industry. Ford is distributing makeup (specifically, eye shadow and nail polish) that complements the colors of its cars. For its part, General Motors is sponsoring cooking classes, offering massages and staging fashion shows as part of its traveling auto displays. Not to be outdone, Toyota has weighed in by pushing its dealers to redecorate their restrooms to be more tasteful, while also constructing in-show-room play areas for the kids.[5]

© AP PHOTO/RIC FIELD

Single women are now the second largest group of homebuyers after couples. Reflecting this trend are the changing demographics of customers at Home Depot and Lowe's, which both indicate that about half of the purchases made in their stores are by women. As a result, both companies have made adjustments to how they market to women.

Home improvement centers, such as Home Depot or Lowes, know that women shoppers are vital to their success. Yet, women feel that these retailers offer an unnecessarily complex shopping process. A recent study found that women want a stress-free experience and want to feel that Lowes and Home Depot appreciate their business. Ninety-seven percent of the women interviewed said that having one person capable of answering all of their questions was one of the most important services a home improvement retailer could provide.[6]

Marriage is a declining institution in America. In the 1950s, the likelihood that someone would be married during his or her lifetime was 95 percent. Today, it's only 85 percent.[7]

Whereas 80 percent of all households in the 1950s included a married couple, just above 50 percent do today. The traditional American family of two adults with kids at home accounted for 40 percent of U.S. households in 1970. Today, that percentage has fallen below 25 percent for the first time ever, and it's projected to be only 20 percent by 2010.[8]

The shift has been to single households, which now outnumber married households with kids. In 1970, the reverse was true by a margin of more than two to one. Single people made up 17 percent of U.S. households in 1970. Today, they account for more than 25 percent, and that percentage is projected to grow to 30 percent by 2010. Already, single people account for 42 percent of the workforce, 40 percent of home buyers, and 35 percent of voters. Single-parent households have also grown from 11 to 16 percent. One-third of children born today have single parents.[9]

Single women now account for 27 percent of all first-time home buyers and 21 percent of the homebuyers overall. This is more than double the rate of 20 years ago.[10] Part of this is due to the fact that women are earning more than ever before. In big cities, such as New York, Boston, Chicago, and Dallas, women under 30 years old are earning more than their male counterparts.[11]

THERE IS NEVER ENOUGH TIME

Research shows that the large percentage of people who say they never have enough time to do all that they need to do keeps inching up. In 2001, it was 73 percent; in 2002, 75 percent; in 2003, 76 percent; in 2004, 77 percent. Year to year, these shifts are unremarkable, but over several years clearly ever more people are worried about having too little time.[12]

COURTESY, BLACKBERRY–BRODEUR WORLDWIDE (FOR RIM)

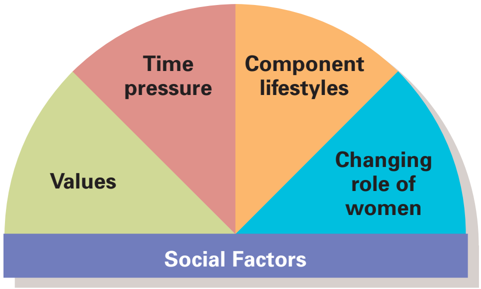
Over 31 percent of college-educated male workers are regularly working 50 or more hours a week, up from 22 percent in 1980. About 40 percent of American adults get less than seven hours of sleep on weekdays, up from 34 percent in 2001. Almost 60 percent of meals are rushed, and 34 percent of lunches are eaten on the run.[13] To manage their scarce time, about 74 percent of working adults engage in multitasking— doing more than one thing at a time.[14] They're talking on their cell phones while rushing to work or school, answering e-mails during conference calls, waking up at 4 A.M., and generally multitasking day and night.

Not only is there not enough time available, but BlackBerrys, cell phones, e-mail, and other high-tech gear are eroding traditional boundaries between the office, school, and home. As a result, most Americans feel that they don't have enough time for their families. But many busy families are learning to turn technology to their advantage, using it to stay in touch and, at the same time, increase family time. Forty-eight percent of working women increased their use of the Internet during 2006. The Internet saves shopping time and enables working women to stay in touch with their families.

Some sociologists are saying that Americans are not the workaholics that we claim to be. Today, these scholars say, we spend far less time on work than Americans did four decades ago. From 1965 to 2003, according to one study published recently, the average American gained the equivalent of seven weeks of vacation—in the form of extra leisure time spread throughout the year. Much of the time-savings comes from a source few people think about when they whine (or brag) about their workweeks; cleaning and cooking. We do much less of it than we used to, thanks to vacuum cleaners, takeout food, and other innovations. And the time-savings there more than offsets the extra time women now spend in offices.[15]

REVIEW LEARNING OUTCOME

LO 2 Describe the social factors that affect marketing



LO 3 Demographic Factors

Another uncontrollable variable in the external environment—also extremely important to marketing managers—is demography, the study of people's vital statistics, such as their age, race and ethnicity, and location. Demographics are significant because the basis for any market is people. Demographic characteristics are strongly related to consumer buyer behavior in the marketplace.

POPULATION[16]

The most basic statistic of all is population because people are directly or indirectly the basis of all markets. The U.S. population is now slightly above 300 million. But it's the 400 million milestone, which the U.S. will reach in about 35 years, that has demographers and economists really talking. Those additional 100 million people, many of them immigrants, will replace aging baby boomers in the work force, fill the Social Security coffers and, in all likelihood, keep the economy vital and life interesting. But they also will further crowd cities and highways, put new strains on natural resources, end the majority status of whites, and probably widen the gulf between society's haves and have-nots.

With about 86 people per square mile nation-wide now, the U.S. would seem to have plenty of room for more. Even after the next 100 million people are added, the U.S. still will have one-sixth the density of Germany, whose population is expected to stop growing within a few years. But those averages hide disparities that could prove worrying. Even as it grows, the population is increasingly concentrating in just a dozen or so states, such as Florida, Texas, North Carolina, and Colorado. North Dakota is losing population, Ohio is adding a mere 20,000 people a year and heartland states like Kansas and Nebraska average fewer than 14 households per square mile.

demography
The study of people's vital statistics, such as their age, race and ethnicity, and location.

More than half the population lives within 50 miles of the coasts. In the next decade, an additional 25 million people—half the total population increase—will join them there. That concentration of population is likely to result in megacities of 25 million or more as people head to them for jobs. Economists predict that market forces eventually will shift some of the U.S. population back to interior states where housing is cheaper, land is more abundant, social services are less stressed and labor is cheaper for businesses.

We turn our attention now to a closer look at age groups, their impact, and the opportunities they present for marketers. The cohorts have been given the names of tweens, Generation Y, Generation X, and baby boomers. You will find that each cohort group has its own needs, values, and consumption patterns.

TWEENS

They watch cable channels designed just for them, they cruise the Net with ease, they know what they want—and often get it. They are America's tweens (today's pre- and early adolescents, ages 9 to 14), a population of more than 20 million. With attitudes, access to information, and sophistication well beyond their years and purchasing power to match, these young consumers will spend over $21 billion in 2008. If one adds in the amount parents spend on tweens, the total spending is estimated as high as $300 billion.[17]

Tweens' styles don't reflect those of their parents. They want their own look. And parents spend about $230 per tween on back-to-school clothes to give them just that.[18] In fact, there is now a clothing line just for the girl tween called "It Chick." It Chick clothing includes sparkly tank tops, dressier tops with satin-bow detailing and cool, retro roller-skate T-shirts. Denim skorts, leggings, and gauchos are also part of the collection. Abercrombie stores, the tween version of Abercrombie & Fitch, features loud, thumping music, blowup posters of young girls and boys, and clothing just for preteens. Clothes are not the only product area that has caught the eye of "tween marketers." Cell phone usage by tweens will be the industry's biggest growth area through 2011. This will be a financial windfall for the carriers because tweens like to do text messaging.[19]

Tweens overwhelmingly (92 percent) recognize television commercials for what they are—"just advertising." About three-quarters regard billboards and radio spots as paid advertising, and about half recognize promotional mediums such as product placements on television shows.[20]

Tweens are not the youngest market that is growing in importance. Pre-tweens, ages 6-9, are moving beyond Chuck E. Cheese. For example, every treatment chair at Peaches & Cream Spa is filled. Feet are buffed, nails meticulously polished and shoulders massaged with hot stones as the sound of female voices fills the room with intense discussion on the issues du jour—which, at the moment, includes speculation on who among them owns the most My Little Pony toys. The clients are all pre-tweens. They are attending a "princess spa birthday party."[21]

TEENS[22]

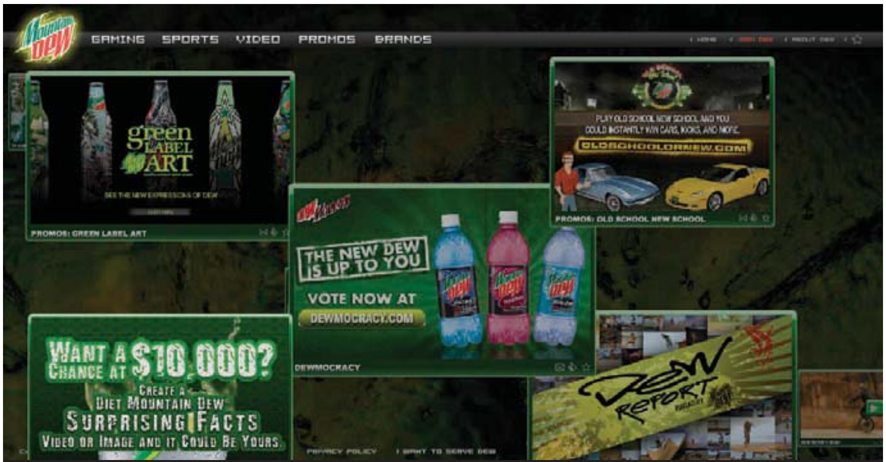
There are approximately 25 million teens in the U.S., and they spend about $195 billion annually. They spend approximately 72 hours per week tuned in electronically. This includes TV, Internet, music, video games, cell phoning, and text messaging. Many teens participate in online social networks, such as MySpace, which has 70 million unique visitors each month. Fully 68 percent of teens have created profiles on MySpace, Zanga, or Facebook.

Little, Brown Books for Young Readers recently promoted an online chat with Clique series author Lisi Harrison via her MySpace page, collecting more than 2,000 questions from readers and attracting 200 teens for the chat session. "One of the main themes in the chat was that the teens really wanted to have an official place where they could talk to each other about the books," says Tina McIntyre, director of marketing at LBYR. So when it came time to revamp the Web site for Stephenie Meyer's Twilight saga, LBYR included message boards to give teens a place to converse, as well as a blog for reviews, media appearances, and photographs. A recent poll on the boards about the heroine's romantic dilemmas that asked, "Who should Bella choose?" racked up more than 6,000 votes.[23]

For teens, shopping has become a social sport. Over 62 percent say that they love to shop. They patronize the big box retailers, such as Best Buy, and luxury brands, with little room for retailers in between. Teens love Armani, Gucci, and Coach. They also go to Taco Bell and drink Coke.

A few more interesting facts about teens:

- The average teen or tween earns about $30.00 per week. A substantial portion of their budget (43 percent) is spent on fashion.
- Teens are multicultural. Four in 10 children ages 5–9 (40 percent) are non-White or Hispanic, as are 38 percent of those ages 15–17.
- Music and entertainment are (still) critical to everyday life. Eight in 10 teens (80 percent) listen to music during their free time.
- Entertainment has to be on-demand for teens. More than 90 percent engage in on-demand media consumption.
- Life revolves around the mall. More than two-thirds of teens go to the mall at least once a week, both to shop and socialize.
- It's not all about new media. The average teen reader spends 43 minutes per day reading.[24]



COURTESY, © PEPSICO

Gen-Yers made Mountain Dew one of the biggest teen soda hits ever. But the drink's success has little to do with advertising. Instead, kids found out about the "Dew" from Gen Y's most trusted endorsers—each other.

GENERATION Y

Those designated by demographics as Generation Y were born between 1979 and 1994. They are about 73 million strong, more than three times as large as Generation X. And though Generation Y is much smaller than the baby boom, which lasted nearly 20 years and produced 78 million children, its members are plentiful enough to put their own footprints on society. Most Gen Yers are the children of baby boomers and hence are also referred to as "echo boomers," or the "millennial generation."

They already spend nearly $200 billion annually and over their lifetimes will likely spend about $10 trillion. Some have already started their careers and are making major purchasing decisions such as cars and homes; at the very least, they are buying lots of computers, MP3 players, cell phones, DVDs, and sneakers.

Researchers have found Gen Yers to be:

Generation Y
People born between 1979 and 1994.

- *Impatient:* Gen Y has grown up in a world that's always been automated, and they've had access to computers, CD-ROMs, the Internet, DVD players, chat rooms, instant messaging, and the like, for as long as they can remember, so it's no surprise that they expect things to be done *now*.
- *Family-oriented*: Unlike Gen X before them, overall Gen Yers had relatively stable childhoods. They also grew up in a very family-focused time when even big companies strived to become more family- and kid-friendly. It's the generation that inspired spin-off stores like babyGap and the makeover of Las Vegas into a family vacation destination.
- *Inquisitive*: Knowing more than their parents about computers and technology has always been a source of pride for the echo boomers. It's led to a natural inquisitiveness that many still possess. They want to know why things happen, how things work, and what they can do next.
- *Opinionated*: From the time they were children, Gen Yers have been encouraged to share their opinions by their parents, teachers, and other authority figures. That's translated to a group who feel that their opinions are always needed and welcomed.
- *Diverse*: This is the most ethnically diverse generation the nation has ever seen, and many don't identify themselves as being only one race. Consequently, they're much more accepting overall of people who are different from themselves.
- *Time managers*: Their entire lives have been scheduled—from playgroups to soccer camp to Little League. So, it's no surprise that they've picked up a knack for planning along the way.
- *"Street Smart"*: The term isn't used in the literal sense, but simply means that these young people have seen a lot. With the Internet and 24-hour cable TV news exposing them to recounts of violence, war, and sexuality at a young age, they're not easily shocked. They're much more aware of the world around them than earlier generations were.[25]

- *Connected*: Fifty-four percent use social networking sites like MySpace or Facebook. And 44 percent have created profiles featuring photos, hobbies, and interests.[26]

Gen Yers want to be financially successful. About 75 percent feel that it is "essential" or "very important" to be well-off financially.[27] While Gen Yers will work a 60-hour week if they have to—and might even do so happily if they're paid enough to make the most of their precious downtime—they don't want that to be a way of life. Some firms where long hours are the norm have found ways to compensate. At Skiadden Arps, new employees are reimbursed up to $3,000 for home-office equipment and $1,000 every year after. And the firm's gyms are a big hit with Gen Yers. "You'd be amazed, when people come by to interview or check out the firm, what a warm response the fitness center gets," says Wallace Schwartz, who leads the firm's New York office.[28]

At accounting firm Ernst & Young, recruiters hand out flash drives instead of brochures, send text messages to schedule meetings with candidates, and give interns video cameras to create vlogs for the firm's Web site. They also launched the first corporate-sponsored recruiting page on Facebook to meet Gen Yers on their own turf.[29]

Generation X
People born between 1965 and 1978.

GENERATION X


© PHOTODISC/GETTY IMAGES

Generation X—people born between 1965 and 1978—consists of 40 million consumers. It was the first generation of latchkey children—products of dual-career households or, in roughly half of the cases, of divorced or separated parents. Gen Xers have been bombarded by multiple media since their cradle days; thus, they are savvy and cynical consumers.

Gen Xers, now in their 30's and 40's, are reaching the age where they are sending their kids off to college. Gen Xers tend to be more protective and involved with their kids than were the baby boomer generation. They highly value the importance of education. Sixty-three percent say they began planning for their kids' college education in elementary school or earlier.[30]

Although Gen Xers are buying homes and spending money to decorate and renovate them, most companies still ignore them, focusing instead on the larger demographic groups—baby boomers and Gen Y. However, some furniture retailers, such as Williams-Sonoma's Pottery Barn and Crate & Barrel, target Gen Xers who want to mix and match different styles. Ethan Allen is now attracting Gen Xers with its new TV ads. Williams-Sonoma also appeals to more Gen Xers with West Elm, its newer furniture concept, which offers edgier designs and lower prices than those found at Pottery Barn.

Gen Xers are avid buyers of the latest clothes, technology, and recreational products. Now that they have advanced in the corporate world, they are demanding certain values from the retailers that they patronize. Gen Xers want frankness, client service, reliability, and authenticity. If retailers aren't true to their word, they quickly lose their Gen X customer.[31]

Gen Xers are careful shoppers when it comes to home furnishings. Some 31 percent of Gen Xers polled said they checked at least four stores before buying, and 65 percent held no loyalty to any retail brand (only 13 percent did) while 41 percent said they'd shop at any store "that had a good deal." Asked what furniture brands come immediately to mind, the largest bloc of respondents (35 percent) said "none," and 70 percent cited brand as the least important factor in buying.[32]

Researchers have found that a male Gen X traveler is more likely than a boomer to pick a hotel with a sports bar. But the pub must be genuine and the workout room cutting edge. So, Holiday Inn Select is adding *Sporting News* Grill restaurants and Fitness by Nautilus workout centers to its offerings. In-room amenities will include Wolfgang Puck coffee, Moen showerheads, and Garden Botanika bath products.

Why does tailoring the merchandise to particular age groups matter? One reason is that each generation enters a life stage with its own tastes and biases, and tailoring products to what customers value is key to sales.

BABY BOOMERS—AMERICA'S MASS MARKET

When Vespa motor scooters came puttering back into the U.S. market in 2000 after a 15-year absence, managers at the Italian company figured their biggest customers would be twentysomethings looking for a cheap way to get around. But executives at Piaggio, Vespa's parent company, noticed something odd as they scootered back and forth to their Manhattan offices: the most enthusiastic sidewalk gawkers were often aging baby boomers who remembered the candy-colored bikes from their youth. It turns out that boomers have lost none of their affection for Vespa. Better yet, now they can afford to buy top-of-the-line models with all the trimmings. Much to the company's surprise, consumers age 50 and older now buy a quarter of the scooters Vespa sells in the United States.

baby boomers
People born between 1946 and 1964.

There are 77 million baby boomers (persons born between 1946 and 1964), making them the largest demographic segment in the population today. The oldest have already turned 60 years old. With average life expectancy at an all-time high of 77.4 years, more and more Americans over 50 consider middle age a new start on life. Fewer than 20 percent say they expect to stop work altogether as they age. Of those who plan to keep working at least part-time, 67 percent said they'll do so to stay mentally active, and 57 percent said to stay physically active. People now in their 50s may well work longer than any previous generation; more than 60 percent of men aged 60 to 64 are expected to be in the workforce in 2012, up from about 54 percent in 1992, according to the Bureau of Labor Statistics.[33]

Boomers' incomes will continue to grow as they keep working. As a group, boomers have more than $2 trillion of spending power a year. They're likely to be vigorous consumers as they empty the nest, take on new jobs, relocate, support the children they had in their 40s, go back to school, start a second or third career, remarry, inherit money from their savings-minded parents, pursue new hobbies, and tackle the health issues of aging.

Many marketers believe that consumers' brand preferences are locked in by age 40. That might have been true for previous generations. But today's over-50 crowd is just as likely, and in some cases more likely, as everyone else to try different brands within a product category. According to Yankelovich, Inc., 33 percent a consumers older than 50 agree that it's "risky" to buy an unfamiliar brand. That's less than the 36 percent of respondents aged 16 to 34 and only a little more than the 30 percent of people aged 35 to 49 who agree with that notion.[34] In some categories such as cosmetics and electronics, older consumers are even more willing to brand-hop than younger ones.


© MICHEL DOOLITTLE/ALAMY

Procter & Gamble's Cover Girl brand, which depends on women older than 55 for about 20 percent of its sales, has just launched its first line of makeup aimed at older women. The name of the product, Advanced Radiance Age-Defying makeup, hints that advancing age can be pretty. And while ads still show a stunningly gorgeous face, that face belongs to an older woman—51-year-old former supermodel Christie Brinkley.

Baby boomers are not a monolithic group. A recent lifestyle study divided this huge market into four segments:

- *"Looking for balance" boomers*: About one-quarter of boomers (27 percent) fall into this very active and busy segment. They represent an excellent market for companies that can offer them time-saving products and services. Though money is important, saving time is equally important to this segment. Companies engaged in travel-related businesses and food-service businesses will find key opportunities here.

- *"Confident and living well" boomers*: Confident and living well boomers represent 23 percent of all boomers. They have the highest incomes of all the segments and relish the chance to be the first to purchase a new product or service. They are technologically oriented and care about what is stylish and trendy. They are the most active boomers, and travel is one of their favorite interests. Marketers offering luxury goods and services will find prime boomer prospects here.
- *"At ease" boomers*: At ease boomers represent 31 percent of all boomers. They are at peace with themselves and do not worry about the future, job security, or financial security. They express the least interest in luxury goods and services and don't travel much. They are the most home-centric and family-oriented segment of the boomers. Marketers of traditional household products and services will find this group of boomers most receptive to their offerings. New products and innovations are least likely to appeal to this group. Established and trusted brand names will resonate most strongly with this boomer segment.
- *"Overwhelmed" boomers*: As the smallest segment of the boomer population, overwhelmed boomers represent less than 20 percent of boomers. This group has the lowest income of all the segments. They worry about the future and their financial security. This segment is also the least active, and health is a big concern for them. They are also the least social boomers, spending little time with family and friends. These boomers are also far less accepting of technology and are well below average on using electronic, digital, and tech products.[35]

Baby boomers also:

Baby boomers are eager to maintain their active lifestyle, so marketers, like Ameriprise, are finding new ways to reach them as they approach retirement.

- Spend more of their current income.
- Continue to depend on their cars and prefer them to taxis or mass transit.
- Spend increasingly larger shares of their income on health care.
- Make TV a key element of their lifestyles.
- Remain in their homes and avoid nursing facilities.
- Are politically conservative.
- Are civically active and wield growing influence.
- Are joiners.
- Spend heavily on housekeeping supplies, household furnishings and equipment, new vehicles, entertainment, computers, healthcare products, vitamins, healthier foods, and reading materials.
- Spend less of their income on apparel, cosmetics and fast food.[36]

Baby boomers, because of the sheer size of the market segment, account for 60 percent of all shopping dollars spent on consumer packaged goods.[37] Baby boomers are also heavily involved in word-of-mouth promotion. When fellow boomers ask them for advice on products and services, 89 percent of them deliver it. And they are likely to seek such a recommendation approximately 90 times per year. Moreover, 93 percent of baby boomers trust their friends for information.[38] Nevertheless, marketers spend countless hours trying to create promotional messages that will resonate with boomers. Here are a few examples:

- *Connecting with boomers' sense of themselves as trailblazers*. At every stage of their lives, boomers have challenged the status quo. Brands that convey a totally new benefit will appeal to boomers' inherent desire to break from the norm. American Express's Ameriprise financial services division expresses it well: "You changed everything that came before you. That was you then... that's still you now."
- *Focusing on their lives, not their ages*. Boomers don't need to be reminded of how old they are getting. Rather than stress their age, Centrum Silver uses advertising to reflect older consumers' passion to continue doing the things they love.
- *Linking the brand with a major life event*. Bayer Aspirin's "Do More" effort builds an emotional bond by telling the story of someone who "had a heart attack and lived"; that's why the person is committed to Bayer.
- *Knowing that boomers are jaded students of ads*. Boomers are idealists, but they grew up with TV ads, and are skeptical of empty promises. The Dove campaign that shows real-looking women instead of models is not just relatable; it preempts boomers' suspicions about exaggerated beauty claims.[39]

Promotion to baby boomers and other demographic segments is not always without controversy. The Ethics in Marketing box explains why.

ETHICS in Marketing

Drug Firms Find That Ad Blitzes Pay Off Big

ETHICS

Drug advertising aimed at consumers is a fast-growing category that reached more than $4.5 billion. The popularity of direct-to-consumer drug advertising continues to grow because it is highly profitable for the pharmaceutical manufacturers. Research has found that for every 10 percent increase in advertising for a given medicine, prescription sales of drugs across the same class rise 1 percent. Other research showed that every extra dollar drug companies spent on ads pushed up revenue by $4.20.

The ad with greatest advertising recall in 2007 was Lunesta with the "luna moth." Over 50 percent of the persons who remember any drug advertising recalled Lunesta. Zyrtec was next, with its "dream house" campaign.

Critics are increasingly concerned that the ads encourage consumers to demand drugs they don't need and that may cause harmful side effects down the road. The only other country that allows direct-to-consumer advertising of pharmaceuticals is New Zealand. Others deem it too dangerous.

Critics and big pharma both agree that firms should hold off advertising a new medicine for an appropriate period of time. This would allow doctors enough time to learn about the risks and benefits of a new medication before television and Web site viewers see an ad and demand a prescription. Twenty-seven members of the pharmaceutical manufacturers organization have endorsed the guidelines, but it is hard to figure exactly how long the delays in advertising will run. Bristol-Myers Squibb has said that it would delay for 12 months. Johnson & Johnson and Pfizer said they would wait six months. The manufacturers group cannot say how other companies have interpreted the guidelines, a spokesman said. But according to TNS Media Intelligence, the companies have actually been waiting 15 months, on average, since the Vioxx debacle. Vioxx was used by over 80 million people worldwide. Merck, the manufacturer withdrew the product from the market because of the potential increased risk for a heart attack. Critics say that even after F.D.A. approval, the full safety profile of a new drug cannot be known until it has been widely used for a number of years.

The Senate Health, Education, Labor and Pensions panel sent to the floor a bill that would let the government, through the Food and Drug Administration, bar the advertising of new drugs for their first two years on the market. Critics say that is a direct assault on the First Amendment, which says "Congress shall make no law... abridging the freedom of speech, or of the press." Critics further warn that, if this bill passes, the people will have less influence over any information government will next try to control or suppress.[40]

Do you think that Congress should completely ban drug advertising to consumers? Should companies have to wait two years before advertising a new drug? Should advertising of drugs for senior citizens be banned? What about drugs for children?

AMERICANS ON THE MOVE

The average U.S. citizen moves every six years—a trend that has implications for marketing. A large influx of people into an area creates many new opportunities for all types of businesses. Conversely, significant out-migration from a city or town may force many of its businesses to move or close down and markets to dry up. Most people who move don't go far, however. Sixty percent stay in their home county, and another 20 percent move to another county in the same state.[41] The remaining 20 percent are part of a new migration trend from the North to the South and West. A belt stretching from North Carolina south to Florida and then west to California is America's region of net in-migration. Over time cities that lose population like Boston, Cleveland, Detroit, Milwaukee, Minneapolis, Philadelphia, and Toledo, Ohio, could have problems paying for things such as health-care services due to a lower tax base. Over the next 20 years, an exodus of 30 million middle-class and affluent households to the South and West will drastically change markets.[42]

In addition to migration within its borders, the United States experiences immigration from other countries. The six states with the highest levels of immigration from abroad are California, New York, New Jersey, Illinois, Texas, and Massachusetts. The presence of large numbers of immigrants in an area creates a need for markets that cater to their unique needs and desires.

REVIEW LEARNING OUTCOME

LO3 Explain the importance to marketing managers of current demographic trends

	Tweens	Gen Y	Gen X	Baby Boom
Age	8 to 14 yrs 29 million	1979–1994 60 million	1965–1978 40 million	1946–1964 77 million

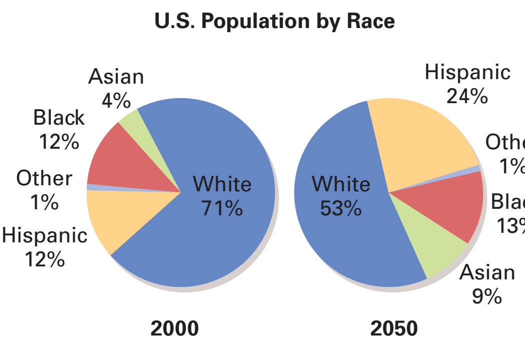
LO4
Growing Ethnic Markets

In 2008, Hispanics wielded more than $1 trillion in spending power, an increase of 340 percent since 1990. In that same year, African Americans' spending topped $921 billion, and Asian Americans' spending power soared over 400 percent since 1990, to $526 billion—far outpacing total U.S. growth in buying power.[43]

Hispanics are America's largest minority group with 12.5 percent of the population followed by African Americans with 12.3 percent and Asian Americans with 3.6 percent.[44] In both Texas and California, minorities now account for over half of the population. The same is also true for Hawaii and New Mexico, but this has been the case for many years. The projected U.S. population by race in 2050 is shown in Exhibit 4.1.

Companies across the United States have recognized that diversity can result in bottom-line benefits. More than ever, diversity is emerging as a priority goal for visionary leaders who embrace the incontestable fact that the United States is becoming a truly multicultural society. Smart marketers increasingly are reaching out and tapping these growing markets. Recently, Pepsi attributed one percentage point of its 7.4 percent revenue growth, or about $250 million, to new products inspired by diversity efforts. Those products included guacamole-flavored Doritos chips and Gatorade Xtremo, aimed at Hispanics, and Mountain Dew Code Red, which tends to appeal to African Americans.[45]

Exhibit 4.1
U.S. Population by Race



SOURCE: U.S. Census Bureau.

MARKETING TO HISPANIC AMERICANS

The term *Hispanic* encompasses people of many different backgrounds. Nearly 60 percent of Hispanic Americans are of Mexican descent. The next largest group, Puerto Ricans, make up just under 10 percent of Hispanics. Other groups, including Central Americans, Dominicans, South Americans, and Cubans, each account for less than 5 percent of all Hispanics.[46]

Wal-Mart has been the largest retailer in Mexico since 2000. But until recently, it has taken a low-key approach to targeting Hispanics in the United States. Now the world's largest retailer is stepping up efforts to attract America's fastest-growing immigrant group.

The diversity of the Hispanic population and the language differences create many challenges for those trying to target this market. Hispanics, especially recent immigrants, often prefer products from their native country. Therefore, many retailers along the southern U.S. border import goods from Mexico. In New York City, more than 6,000 *bodegas* (grocery stores) sell such items as plantains, chorizo (pork sausage), and religious candles to Puerto Rican Americans. The *bodegas* also serve as neighborhood social centers. Fresh produce is usually very important to Hispanics because of the tradition of shopping every day at open-air produce markets in their native country.

In general, Hispanics tend to be very brand loyal, but they often are not aware of many mainstream U.S. brands. Instead, many Hispanics are loyal to the brands found in their homeland. If these are not available, Hispanics will choose brands that reflect their native values and culture. This preference for brands from home has helped Mexico's Jarritos become one of the fastest-growing soft drinks in the United States. Yet until recently it was *una marca desapareciendo*—a dying brand. Despite having name recognition in its homeland that rivaled that of Coca-Cola, the 55-year-old soda was losing ground to imported U.S. rivals. So parent company Novamex boldly crossed the border. In the past few years, it has moved onto the competition's turf with marketing that speaks to Mexican Americans' thirst for the good old days. Today, Jarritos's 11 flavors are sold in more than 50,000 U.S. outlets. Sales at privately held Novamex, which now distributes 11 Mexican brands, are set to grow 23 percent this year to an estimated $225 million, thanks mostly to Jarritos.[47]

Wal-Mart has been the largest retailer in Mexico since 2000. But until recently, it has taken a low-key approach to targeting Hispanics in the United States. Now the world's largest retailer is stepping up efforts to attract America's fastest-growing immigrant group. In 2004, Wal-Mart began printing its monthly ad circulars in English and Spanish. It also launched its own Hispanic magazine, called *Viviendo* (Living), which it distributes free at 1,300 stores heavily shopped by Hispanics. The glossy quarterly magazine features profiles of Latino leaders and celebrities next to ads highlighting Wal-Mart's expanding line of products and services geared toward Hispanics.

In another move, Wal-Mart recently teamed up with Sprint to offer a new prepaid wireless service expressly targeted to Hispanics. Wal-Mart is also stocking a line of bathroom and tabletop accessories from New York restaurateur and cookbook author Zarela Martinez, whose designs are inspired by Mexican folk art and culture. And Wal-Mart's three-year-old financial-services department offers cut-rate fees on money wire transfers, a big lure for immigrants who support family back home.[48]

About 68 percent of U.S. Hispanics have home Internet access. Hispanics who use the Internet are, on average, much younger than the general online population. Sixty-three percent of Hispanics who have Internet access use the Web to look for information, rather than to play games or hang out in chat rooms, versus 52 percent of the general population.[49] Kraft Foods has realized that the Net is a good way to connect with Hispanics. The company launched **http://www.comidakraft.com,** where Hispanics can share or post their recipes online, through what's called the Recipe Connection. The Recipe Connection page encourages Hispanic consumers to submit a favorite recipe containing at least one Kraft food product, "perhaps one that has been passed down in your family or an original creation from your own kitchen." Many of the recipes later appear in the magazine, *comida y familia,* a Spanish-language recipe index published by Kraft.

Marketers have found that simply having TV programs in Spanish is not sufficient to attract the target market. It must also be meaningful to their culture. Previously, MTV en Español was just that—traditional MTV in Spanish. The program today is called MTV Tr3s, which is bilingual (subtitles appear in Spanish where it is spoken) and features shows like *Quiero Mis Quinces* about *quinceañera* (15th birthday) parties and *Pimpeando,* about car culture.

"MTV is now taking a deeper look at how to connect with Latinos," said Carl Kravets, chairman/president at the Association of Hispanic Advertising Agencies and chairman at marketing firm Cruz/Kravetz Ideas, Los Angeles. "It's not just about language and music but about connecting with youth with relevant lifestyle issues important to them."[50]

MARKETING TO AFRICAN AMERICANS

Many firms are creating new and different products for the African American market. Often entrepreneurial African Americans are the first to realize unique product opportunities. For example, when Yla Eason couldn't find an African American superhero doll to buy for her son, she founded Olmec Corporation. Now this New York-based toy manufacturer is a $2 million company, marketing more than 60 kinds of African American and Hispanic dolls. Eason has a distribution partnership with Hasbro.

Several companies owned by African Americans—such as Soft Sheen, M&M Johnson, and ProLine—target the African American market for health and beauty aids. Huge corporations like Revlon, Gillette, and Alberto-Culver have either divisions or major product lines for this market as well. Alberto-Culver's hair-care line for this segment includes 75 products. In fact, hair-care items are the largest single category in the African American health and beauty aid industry. Maybelline with its Shades of You product line has the largest share (28 percent) of the African American health and beauty aid market.

An effective way to reach a specific segment of the African-American market is to create a nontraditional marketing campaign. For example, Merrill Lynch hosts community-based events. Recently, the financial services firm sponsored a cultural exhibition, Lasting Foundations: The Art of Architecture in Africa, at the National Building Museum in New York. There, the company took the opportunity at the exhibition to invite about 300 prospective clients and guests for a preview. More than 25 financial advisers acted as guides to their guests throughout the evening. "We had the financial advisers invite clients and prospects and gather them together and provoke a dialogue with them," said a Merrill Lynch spokeswoman.[51]

Allstate has been targeting black consumers for several decades. Each year it spends more of its advertising budget to reach the African American market. Allstate offers *The Black Enterprise African American Travel Guide* and gives away Allstate-branded hand fans, extolling Allstate's aid to black families, at churches with predominantly black congregations. The African American twist Allstate adds to its "You're in good hands . . ." tagline is the connotation, "Only Allstate respects you enough to give you the insurance experience you truly deserve."[52]

The promotional dollars spent on African Americans continue to rise, as does the number of black media choices. BET, the black cable TV network, has 76 million viewers.[53] The 36-year-old *Essence* magazine reaches one-third of all black females ages 18 to 49. But radio holds a special appeal. African Americans spend considerable time with radio (an astounding 4 hours a day versus 2.8 hours for other groups), and urban audiences have an intensely personal relationship with the medium. ABC Radio Network's Tom Joyner reaches an audience of more than 8 million in 115 markets, and Doug Banks is heard by 1.5 million listeners in 36 markets. Pepsi used radio to raise the level of Mountain Dew awareness and its market share in urban markets. Artists like Busta Rhymes personify the image of Mountain Dew and create the lyrics and the vibe that sells the product.

Coca Cola recently used the TV program, American Idol, to target black consumers. The new ads, entitled "Timeline," feature a series of milestones in black history complemented by images which illustrate the progression of the Coca-Cola contour bottle over time. "'Timeline' pays respect to the many incredible contributions that African Americans have made to culture, science and community," said Anne Sempowski Ward, assistant vice president, African American Marketing, Coca-Cola North America. "This special salute honors the past and inspires optimism for the future, and reminds people that Coca-Cola was there to celebrate these landmark achievements."[54]

MARKETING TO ASIAN AMERICANS

Asian Americans, who represent only 4.2 percent of the U.S. population, have the highest average family income of all groups. At $66,500, it exceeds the average U.S. household income by more than $10,000. Sixty percent of all Asian Americans have at least a bachelor's degree.[55]

Because Asian Americans are younger and better educated and have higher incomes than average, they are sometimes called a "marketer's dream." Not only is their purchasing power expected to grow, but as a group, Asian Americans are more comfortable with technology than the general population is. They are far more likely to use automated teller machines, and many more of them own the latest electronic gear, such as the i Phone.

A number of products have been developed specifically for the Asian American market. For example, Kayla Beverly Hills salon draws Asian American consumers because the firm offers cosmetics formulated for them. Anheuser-Busch's agricultural products division targets the Asian American market with eight varieties of California-grown rice, each with a different label, to cover a range of nationalities and tastes.

Cultural diversity within the Asian American market complicates promotional efforts. "There really isn't one Asian American market," says Nancy Shimamoto of San Francisco-based Hispanic & Asian Marketing Research, Inc., a division of Cheskin.[56] Instead, she says, marketers must recognize the cultural and linguistic differences that exist among the markets. "There is absolutely no common language or culture, and to find the ties that bind is extraordinarily difficult," she says.[57]

Some of the major cultural differences among key groups of Asian Americans are:

- CHINESE

  Largest Asian American segment
  Four distinct geographic areas in Chinese category: Taiwan, Hong Kong, People's Republic of China, and Southeast Asia
  Two major dialects: Mandarin and Cantonese
  May be cautious in personal and business dealings
  Tend to be price-conscious
  Embrace idea of planning for long term
  Strong emphasis on family and education

- FILIPINO

  Second largest Asian American segment
  High rate of U.S. acculturation due to English competency
  Heritage/cultural values that are similar to Hispanic culture
  Strong sense of family and community preservation
  Highly religious (predominately Roman Catholic)

- ASIAN INDIAN

  Third largest Asian American segment
  Speak many different languages, and come from a variety of Indian cultural and religious backgrounds

National heritage, culture and values very important

Extreme emphasis on education

Highly price/value conscious

Very loyal to strong brands

Respond best to advertising in English, with Indian national cultural values woven in seamlessly

- VIETNAMESE

Fourth largest Asian American segment

Large number of immigrants were refugees

Quality-conscious and value seekers

Strong political beliefs

Extremely strong tendency for cultural and community preservation

Strong emphasis on family and education

- KOREAN

Fifth largest Asian American segment

Most homogeneous of top Asian subgroups, with the majority of Korean Americans coming from similar socioeconomic backgrounds in Korea

Most likely of all Asian American segments to have immigrated as complete family units

May be more emotional in decision-making

Prefer name brands to lower prices

Independent and aggressive

Strong emphasis on family and education

- JAPANESE

Sixth largest Asian American segment

Highest percentage of U.S.-born individuals of any Asian American segment (due to waves of immigration dating back to the mid-1800s)

A critical mass of Japanese temporary residents in the United States, to establish a subculture; includes students, temporary workers and trainees, and expatriate business families

Tend to value group consensus over individual opinion

Value name brands over price

Strong emphasis on family and education[58]

Although Asian Americans embrace the values of the larger U.S. population, they also hold on to the cultural values of their particular subgroup. Consider language. Many Asian Americans, particularly Koreans and Chinese, speak their native tongue at home. Filipinos are far less likely to do so. Cultural values are also apparent in the ways different groups make big-ticket purchases. In Japanese American homes, the husband alone makes the decision on such purchases nearly half the time; the wife decides only about 6 percent of the time. In Filipino families, however, wives make these decisions a little more often than their husbands do, although by far the most decisions are made by husbands and wives jointly or with the input of other family members.[59]

Asian Americans like to shop at stores owned and managed by other Asian Americans. Small businesses such as flower shops, grocery stores, and appliance stores are often best equipped to offer the products that Asian Americans want. For example, at first glance the Ha Nam supermarket in Los Angeles's Koreatown might be any other grocery store. But next to the Kraft American singles and the State Fair corn dogs are jars of whole cabbage kimchi. A snack bar in another part of the store cooks up aromatic mung cakes, and an entire aisle is devoted to dried seafood.

One American food product held in high esteem is Spam (no, not what you receive in your email inbox). Hormel's Spam was offered as a fresh meat substitute to soldiers during World War II. In South Korea, wedding couples are said to have a long and prosperous life if they receive a wedding pack of Spam. In Hawaii, Spam is sold at McDonald's restaurants, and travel agents send tours packed with Hawaiian residents on annual pilgrimages to the Spam Museum in Austin, Minnesota.[60]

ETHNIC AND CULTURAL DIVERSITY

multiculturalism
When all major ethnic groups in an area—such as a city, county, or census tract—are roughly equally represented.

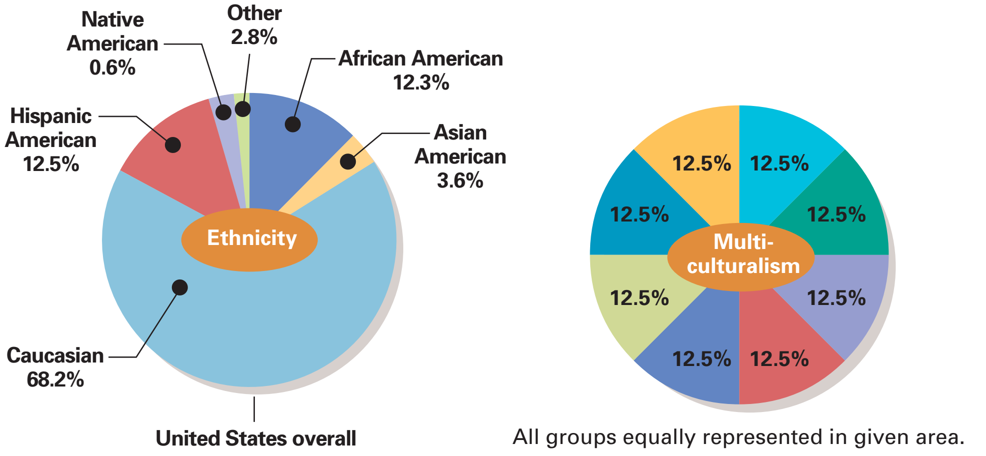
Multiculturalism occurs when all major ethnic groups in an area—such as a city, county, or census tract—are roughly equally represented. Because of its current demographic transition, the trend in the United States is toward greater multiculturalism.

San Francisco County is the most diverse county in the nation. The proportions of major ethnic groups are closer to being equal there than anywhere else. People of many ancestries have long been attracted to the area. Elsewhere, however, a careful examination of the statistics from the latest U.S. Census Bureau reveals that the nation's minority groups, especially Hispanics and Asians, are heavily clustered in selected regions and markets. Rather than witnessing the formation of a homogeneous national melting pot, we are seeing the creation of numerous mini-melting pots, while the rest of America remains much less diverse.

In a broad swath of the country, the minority presence is still quite limited. America's racial and ethnic patterns have taken on distinctly regional dimensions. Hispanics dominate large portions of counties in a span of states stretching from California to Texas. Blacks are strongly represented in counties of the South as well as selected urban areas in the Northeast and Midwest. The Asian presence is relatively small and highly concentrated in a few scattered counties, largely in the West. And Native Americans are concentrated in select pockets in Oklahoma, the Southeast, the upper Midwest, and the West. Multiethnic counties are most prominent in California and the Southwest, with mixes of Asians and Hispanics, or Hispanics and Native Americans.

REVIEW LEARNING OUTCOME

LO4 Explain the importance to marketing managers of multiculturalism and growing ethnic markets



LO5

Economic Factors

In addition to social and demographic factors, marketing managers must understand and react to the economic environment.

The three economic areas of greatest concern to most marketers are consumers' incomes, inflation, and recession.

CONSUMERS' INCOMES

As disposable (or after-tax) incomes rise, more families and individuals can afford the "good life." In recent years, however, U.S. incomes have risen at a rather slow pace. After adjustment for inflation, the median household income in the United States in 2008 was projected to be approximately $49,000. This means half of all U.S. households earned less and the other half earned more.[61]

Education is the primary determinant of a person's earning potential. For example, only 1 percent of those with only a high school education earn over $100,000 annually. By comparison, 13 percent of college-educated workers earn six figures or more.[62] Along with "willingness to buy," or "ability to buy," income is a key determinant of target markets. A marketer who knows where the money is knows where the markets are. If you are seeking a new store location for Dollar General, a retail chain that caters to lower-income consumers, you would probably concentrate on the South and Midwest because most households with annual incomes of less than $45,000 are concentrated in these areas.

The U.S. Census Bureau normally deals in very big numbers, such as the richest one percent of the households (719,910 of them) have an average annual income of $326,720.[63] Sometimes, however, the Census Bureau puts the U.S. economy under a microscope. Here are a few key findings from the most current census.

- In ranking larger American cities, the Census Bureau found San Jose, California and Plano, Texas, had the highest median incomes, at around $71,000, while Miami and Cleveland had the lowest, with median incomes below $25,000.
- Cleveland also had the highest poverty rate for big cities at 32.4 percent, followed closely by Detroit, two cities suffering from the downturn in the American automobile industry and manufacturing.
- Camden, New Jersey, a city struggling with crime, had a poverty rate of 44 percent, the highest number among small-to-midsize cities—but so, too, did College Station, Texas, home of Texas A&M University.
- Among counties with populations of more than 250,000, the three where the households had the highest median incomes were in suburban Washington, D.C.—Loudoun and Fairfax counties in Virginia and Howard County in Maryland.
- The ratio of single men to single women between ages 15 and 44 last year was highest in Nevada (120.2 per 100 women), North Dakota (120.1) and Alaska (118.9). It was lowest in the District of Columbia (93.4).[64]

The Financial Power of Women

Another trend in consumers' income is the growing financial power of women in the United States. Women bring in half or more of the income in the majority of U.S. households, and women control 51.3 percent of the private wealth in the United States. Women also control most of the spending in U.S. households—about 80 percent.[65] And, women have become the primary buyers of many types of products including those that are historically male-dominated products. For example, women purchase:

- 68 percent of new cars
- 66 percent of computers

- 60 percent of home improvements
- 53 percent of investments
- 51 percent of consumer electronics[66]

PURCHASING POWER

purchasing power
A comparison of income versus the relative cost of a set standard of goods and services in different geographic areas.

inflation
A measure of the decrease in the value of money, expressed as the percentage reduction in value since the previous year.

Rising incomes don't necessarily mean a higher standard of living. Increased standards of living are a function of purchasing power. Purchasing power is measured by comparing income to the relative cost of a set standard of goods and services in different geographic areas, usually referred to as the cost of living. Another way to think of purchasing power is income minus the cost of living (i.e., expenses). In general, a cost of living index takes into account housing, food and groceries, transportation, utilities, health care, and miscellaneous expenses such as clothing, services, and entertainment. Homefair's salary calculator uses these metrics when it figures that the cost of living in New York City is almost three times the cost of living in Youngstown, Ohio. This means that a worker living in New York must earn nearly $279,500 to have the same standard of living as someone making $100,000 in Youngstown.

When income is high relative to the cost of living, people have more discretionary income. That means they have more money to spend on nonessential items (in other words, on wants rather than needs). This information is important to marketers for obvious reasons. Consumers with high purchasing power can afford to spend more money without jeopardizing their budget for necessities, like food, housing, and utilities. They also have the ability to purchase higher-priced necessities, for example, a more expensive car, a home in a more expensive neighborhood, or a designer handbag versus a purse from a discount store.

One factor that has been sapping purchasing power has been the rising price of gasoline. The average American household spends five percent of its pretax annual income on gasoline.[67] As a result of the increase in gasoline prices, 67 percent of shoppers will shop for several items at one store instead of driving around, 66 percent make price comparisons, 64 percent do research before making a purchase, and 63 percent wait for sales.[68] Other things that consumers are doing to save money are shown in Exhibit 4.2.

INFLATION

Inflation is a measure of the decrease in the value of money, generally expressed as the percentage reduction in value since the previous year, which is the rate of inflation. Thus, in simple terms an inflation rate of 5 percent means you will need 5 percent more units of money than you would have needed last year to buy the same basket of products. If inflation is 5 percent, you can expect that, on average, prices have risen by about 5 percent since the previous year. Of course, if pay raises are matching the rate of inflation, then employees will be no worse off in terms of the immediate purchasing power of their salaries.

In times of low inflation, businesses seeking to increase their profit margins can do so only by increasing their efficiency. If they significantly increase prices, no one will purchase their goods or services. In more inflationary times, marketers use a number of pricing strategies to cope. (See Chapter 20 for more on these strategies.) But in general, marketers must be

Exhibit 4.2

What Consumers Are Now Doing to Save Money

Opting to do it themselves (lawn care, house cleaning)	68 percent
Turning the thermostat down or up	65 percent
Eating out less often	59 percent
Buying fewer new clothes	59 percent
Fixing items that are broken versus replacing them	56 percent
Cutting back on drinking alcohol and smoking	50 percent
Choosing less expensive restaurants	42 percent
Purchasing cheaper brands	36 percent
Engaging in leisure activities closer to home	31 percent

SOURCE: *Yankelovich*

aware that inflation causes consumers to either build up or diminish their brand loyalty. In one research session, a consumer panelist noted, "I used to use just Betty Crocker mixes, but now I think of either Betty Crocker or Duncan Hines, depending on which is on sale." Another participant said, "Pennies count now, and so I look at the whole shelf, and I read the ingredients. I don't really understand, but I can tell if it's exactly the same. So now I use this cheaper brand, and honestly, it works just as well." Inflation pressures consumers to make more economical purchases. Nevertheless, most consumers try hard to maintain their standard of living.

In creating marketing strategies to cope with inflation, managers must realize that, regardless of what happens to the seller's cost, the buyer is not going to pay more for a product than the subjective value he or she places on it. No matter how compelling the justification might be for a 10 percent price increase, marketers must always examine its impact on demand. Many marketers try to hold prices level for as long as is practical.

RECESSION

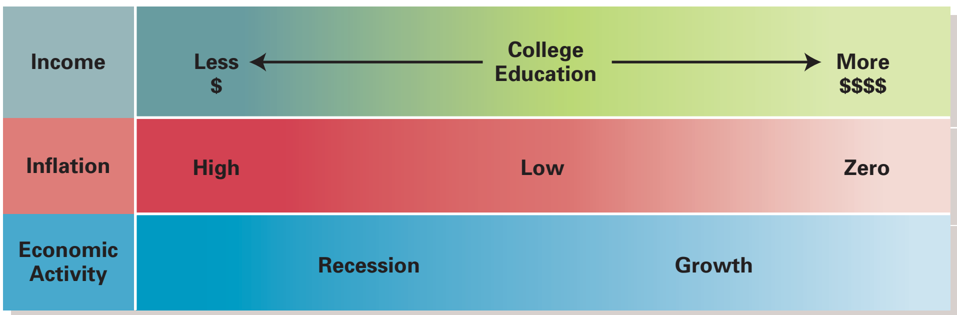
recession
A period of economic activity characterized by negative growth, which reduces demand for goods and services.

A recession is a period of economic activity characterized by negative growth, which reduces demand for goods and services. During a recession, the growth rates of income, production, and employment all fall below zero percent. For example, in a true recession, you wouldn't just receive a smaller raise than in previous years; your pay would actually be cut. In 2001, the slowdown in the high-tech sector, overextended consumer credit, and the terrorist attacks on America resulted in the economy slipping into a recession that lasted until early 2003. The problems of inflation and recession go hand in hand, yet recession requires different marketing strategies:

- *Improve existing products and introduce new ones*: The goal is to reduce production hours, waste, and the cost of materials. Recessions increase the demand for goods and services that are economical and efficient, offer value, help organizations streamline practices and procedures, and improve customer service.
- *Maintain and expand customer services*: In a recession, many organizations postpone the purchase of new equipment and materials. Sales of replacement parts and other services may become an important source of income.
- *Emphasize top-of-the-line products and promote product value*: Customers with less to spend will seek demonstrated quality, durability, satisfaction, and capacity to save time and money. High-priced, high-value items consistently fare well during recessions.

REVIEW LEARNING OUTCOME

LO5 Identify consumer and marketer reactions to the state of the economy



LO6
Technological Factors

Sometimes new technology is an effective weapon against inflation and recession. New machines that reduce production costs can be one of a firm's most valuable assets. The power of a personal-computer microchip doubles about every 18 months. Our ability, as a nation, to maintain and build wealth depends in large part on the speed and effectiveness with which we invent and adopt machines that lift productivity. For example, coal mining is typically thought of as unskilled, backbreaking labor. But visit the Twentymile Mine near Oak Creek, Colorado, and you will find workers with push-button controls who walk along massive machines that shear 30-inch slices from an 850-foot coal wall. Laptop computers help miners track equipment breakdowns and water quality.

RESEARCH

basic research
Pure research that aims to confirm an existing theory or to learn more about a concept or phenomenon.

applied research
An attempt to develop new or improved products.

The United States excels at both basic and applied research. Basic research (or *pure research*) attempts to expand the frontiers of knowledge but is not aimed at a specific, pragmatic problem. Basic research aims to confirm an existing theory or to learn more about a concept or phenomenon. For example, basic research might focus on high-energy physics. Applied research, in contrast, attempts to develop new or improved products. The United States has dramatically improved its track record in applied research. For example, the United States leads the world in applying basic research to aircraft design and propulsion systems.

Rather than invention for the sake of invention, many firms are turning to the marketing concept to guide their research. To give its scientists guidance, Dow first interviews customers to find out their wants and needs. A wish list of products and/or technical characteristics helps the scientists create inventions with market value. Dow recently created a fiber called XLA after learning that apparel makers wanted a "soft stretch" fiber with a natural feel. Dow thinks that the product might deliver sales of $300 million within ten years.

Although developing new technology internally is a key to creating and maintaining a long-term competitive advantage, external technology is also important to managers for two reasons. First, by acquiring the technology, the firm may be able to operate more efficiently or create a better product. Second, a new technology may render your existing products obsolete.

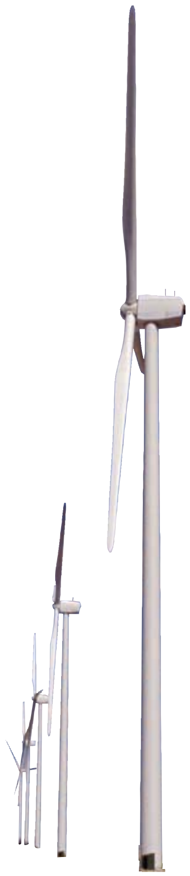
An example of operating more efficiently by using external technology is UPS. Not so long ago, UPS drivers worked off maps, 3 × 5 note cards, and their own memory to figure out the best way to run their routes. That changed when UPS began to implement a $600 million route optimization system—think MapQuest on steroids—that each evening maps out the next day's schedule for the majority of its 56,000 drivers. So sophisticated is the software that it designs each route to minimize the number of left turns, thus reducing the time and gas that drivers waste idling at stoplights. The latest wrinkle: a new feature that, with the aid of global positioning system technology, warns drivers with a beep if they pull into the wrong driveway. It also enables UPS to send a driver more quickly after you call in a pickup since dispatchers know exactly which driver is closest. And in 2008, UPS plans to use its package-flow technology to launch a service that allows customers to reroute a package in transit to a different address.[69]

GLOBAL INNOVATION

Microsoft spent $80 million to open an Advanced Technology Center outside Beijing, China. With nearly 500 engineers, Ph.D. students, and visiting professors, it is one of Microsoft's most important facilities for developing graphics, handwriting-recognition, and voice-synthesizing technologies. The technology center illustrates how innovation is increasingly becoming a global process conducted at worldwide research and development operations. Like Microsoft, IBM has facilities around the world including major labs in China, Israel, Switzerland, Japan, and India.

General Electric has become a leader in wind energy technology by tapping into a global network. The technology for GE's new wind turbines comes from the following countries:

- *United States*: The main research center in Niskayuna, New York, handles basic research, while other centers in New York, Pennsylvania, South Carolina, California, and Virginia tackle other design and engineering aspects.
- *Canada*: Engineers at GE Consumer & Industrial in Peterborough, Ontario, provided the manufacturing technology for the generator.
- *India*: Researchers at Bangalore have crafted a series of analytical models and turbine system design tools that affect the entire turbine.
- *China*: Researchers in Shanghai are in charge of the turbine simulator to test new products and conduct high-end tests for variable-speed power electronics.
- *Germany*: The lead experts on the gearbox work at GE Wind operations in Salzbergen. Researchers in Munich design sensors and monitor advanced controls.[70]



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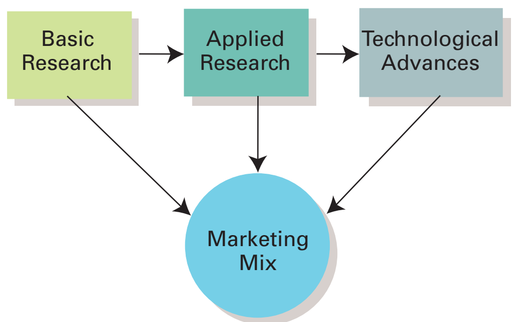
INNOVATION CARRIES TO THE BOTTOM LINE

Innovation pays off big for creative organizations. The 25 most innovative firms in the world achieved an average profit margin growth of 3.4 percent per year since 1995. This compares with 0.4 percent for the average Standard & Poor's Global 1200 company.[71] Innovation allows companies to grow faster and have a richer product mix. The twenty most innovative companies in the world are shown in Exhibit 4.3.

REVIEW LEARNING OUTCOME

LO6 Identify the impact of technology on a firm



LO7
Political and Legal Factors

Business needs government regulation to protect innovators of new technology, the interests of society in general, one business from another, and consumers. In turn, government needs business because the marketplace generates taxes that support public efforts to educate our youth, pave our roads, protect our shores, and so on. The private sector also serves as a counterweight to government. The decentralization of power inherent in a private-enterprise system supplies the limitation on government essential for the survival of a democracy.

Every aspect of the marketing mix is subject to laws and restrictions. It is the duty of marketing managers or their legal assistants to understand these laws and conform to them because failure to comply with regulations can have major consequences for a firm. Sometimes just sensing trends and taking corrective action before a government agency acts can help avoid regulation. The tobacco industry failed to do this. As a result, Joe Camel and the Marlboro Man are fading into the sunset along with other strategies used to promote tobacco products.

The challenge is not simply to keep the marketing department out of trouble, however, but to help it implement creative new programs to accomplish marketing objectives. It is all too easy for a marketing manager or sometimes a lawyer to

Exhibit 4.3

The World's Most Innovative Companies

Ranking 1—Apple: Apple is a master of product and store design. Now that it's invading the cell-phone market, will it continue its winning streak?

Ranking 2—Google: It didn't invent search advertising, but lifted it to its current heights. Google's famously chaotic innovation process has plunged it into everything from radio ads to online office software.

Ranking 3—Toyota Motor: Toyota's dominance in hybrids could lead to the first plug-in electric auto. Now the No. 1 carmaker, its continuous improvement process is copied worldwide.

Ranking 4—General Electric: CEO Jeff Immelt's push for "imagination breakthroughs," or growth opportunities of $50 million to $100 million, are increasingly leading GE into emerging markets and green technology.

Ranking 5—Microsoft: To some, Microsoft is more fast follower than leading innovator. Still, the software giant's massive R&D budget generates creations that help ensure the popularity of Windows and Office.

Ranking 6—Procter & Gamble: After years of scouting for new products outside its walls, P&G has mapped the innovation strengths of global regions. CEO A.G. Lafley is pushing for more disruptive new ideas.

Ranking 7—3M: The legendary Post-it Note is just one of 3M's many creations, which include everything from dental fillings to roofing shingles. Next on its list: diagnostic tests for infectious diseases.

Ranking 8—Walt Disney: CEO Bob Iger is refueling Disney's creative culture. Moves such as putting ABC shows on iTunes and acquiring Pixar helped move Disney up.

Ranking 9—IBM: The tech services behemoth held an online brainstorm with 150,000 people to dream up new ideas. It hosts annual symposia with outsiders to collaborate on forecasting.

Ranking 10—Sony: This traditional tech hardware maker is devoting more resources to software. To turn its PlayStation 3 console from living-room box into virtual gateway, it created a 3D online world.

Ranking 11—Wal-Mart Stores: Wal-Mart is struggling with growth, but its "green" actions, such as using its leverage as the world's largest retailer to cut suppliers' packaging waste, helped it make the top 20.

Ranking 12—Honda Motor: Headed by a former R&D chief, Honda has been known for its fuel-efficient cars. But its environmental approach isn't limited to autos. Next up: solar panels and a fuel-sipping jet.

Ranking 13—Nokia: To build sales in emerging markets, managers spend time in the homes of local customers. This has led to features for illiterate users such as an icon-driven handset directory.

Ranking 14—Starbucks: The coffee chain's 50-person R&D group created eight new flavors in one year. It also started its own music label and partnered with outsiders to publish books and produce movies.

Ranking 15—Target: Target stands out from its discount rivals by selling designer-inspired products. Innovative marketing, such as buying all the ads in one issue of *The New Yorker*, has also set it apart.

Ranking 16—BMW: BMW is flat, flexible, and fast-reacting. Employees are urged to "break the rules" to cut costs or push through winning ideas, such as the Z4 coupe, which higher-ups initially nixed.

Ranking 17—Samsung Electronics: Samsung stays ahead with intensive investment in new facilities and production systems. These days, it's focusing on the convergence of technologies and phone features.

Ranking 18—Virgin Group: Most of its businesses, such as credit card or mobile virtual networks, are collaborative; Virgin supplies the branding and customer service while partners put up much of the cash.

Ranking 19—Intel: The world's largest chipmaker, Intel is making a big headway in selling to the health care market. It recently previewed its most powerful chip to date and is planning a $2.5 billion plant in China.

Ranking 20—Amazon: The online retailer is now innovating its business model, turning its backroom operations into a digital utility that rents out computer power and warehouse space to other firms.

SOURCE: "Jena McGregor, "Most Innovative Companies," *Business Week,* May 14, 2007, p. 55.

say "no" to a marketing innovation that actually entails little risk. For example, an overly cautious lawyer could hold up sales of a desirable new product by warning that the package design could prompt a copyright infringement suit. Thus, it is important to have a thorough understanding of the laws established by the federal government, state governments, and regulatory agencies to govern marketing-related issues.

FEDERAL LEGISLATION

Federal laws that affect marketing fall into several categories. First, the Sherman Act, the Clayton Act, the Federal Trade Commission Act, the Celler-Kefauver Antimerger Act, and the Hart-Scott-Rodino Act were passed to regulate the competitive environment. Second, the Robinson-Patman Act was designed to regulate pricing practices. Third, the Wheeler-Lea Act was created to control false advertising. These key pieces of legislation are summarized in Exhibit 4.4. The primary federal laws that protect consumers are shown in Exhibit 4.5.

STATE LAWS

Legislation that affects marketing varies state by state. Oregon, for example, limits utility advertising to 0.5 percent of the company's net income. California has forced industry to improve consumer products and has enacted legislation to lower the energy consumption of refrigerators, freezers, and air conditioners. Several states, including New Mexico and Kansas, are considering levying a tax on all in-state commercial advertising.

REGULATORY AGENCIES

Although some state regulatory bodies actively pursue violators of their marketing statutes, federal regulators generally have the greatest clout. The Consumer Product Safety Commission, the Federal Trade Commission, and the Food and Drug Administration are the three federal agencies most directly and actively involved in

Exhibit 4.4

Primary U.S. Laws That Affect Marketing

LEGISLATION	IMPACT ON MARKETING
Sherman Act of 1890	Makes trusts and conspiracies in restraint of trade illegal; makes monopolies and attempts to monopolize a misdemeanor.
Clayton Act of 1914	Outlaws discrimination in prices to different buyers; prohibits tying contracts (which require the buyer of one product to also buy another item in the line); makes illegal the combining of two or more competing corporations by pooling ownership of stock.
Federal Trade Commission Act of 1914	Created the Federal Trade Commission to deal with antitrust matters; outlaws unfair methods of competition.
Robinson-Patman Act of 1936	Prohibits charging different prices to different buyers of merchandise of like grade and quantity; requires sellers to make any supplementary services or allowances available to all purchasers on a proportionately equal basis.
Wheeler-Lea Amendments to FTC Act of 1938	Broadens the Federal Trade Commission's power to prohibit practices that might injure the public without affecting competition; outlaws false and deceptive advertising.
Lanham Act of 1946	Establishes protection for trademarks.
Celler-Kefauver Antimerger Act of 1950	Strengthens the Clayton Act to prevent corporate acquisitions that reduce competition.
Hart-Scott-Rodino Act of 1976	Requires large companies to notify the government of their intent to merge.

Exhibit 4.5

Primary U.S. Laws Protecting Consumers

LEGISLATION	IMPACT ON MARKETING
Federal Food and Drug Act of 1906	Prohibits adulteration and misbranding of foods and drugs involved in interstate commerce; strengthened by the Food, Drug, and Cosmetic Act (1938) and the Kefauver-Harris Drug Amendment (1962).
Federal Hazardous Substances Act of 1960	Requires warning labels on hazardous household chemicals.
Kefauver-Harris Drug Amendment of 1962	Requires that manufacturers conduct tests to prove drug effectiveness and safety.
Consumer Credit Protection Act of 1968	Requires that lenders fully disclose true interest rates and all other charges to credit customers for loans and installment purchases.
Child Protection and Toy Safety Act of 1969	Prevents marketing of products so dangerous that adequate safety warnings cannot be given.
Public Health Smoking Act of 1970	Prohibits cigarette advertising on TV and radio and revises the health hazard warning on cigarette packages.
Poison Prevention Labeling Act of 1970	Requires safety packaging for products that may be harmful to children.
National Environmental Policy Act of 1970	Established the Environmental Protection Agency to deal with various types of pollution and organizations that create pollution.
Public Health Cigarette Smoking Act of 1971	Prohibits tobacco advertising on radio and television.
Consumer Product Safety Act of 1972	Created the Consumer Product Safety Commission, which has authority to specify safety standards for most products.
Child Protection Act of 1990	Regulates the number of minutes of advertising on children's television.
Children's Online Privacy Protection Act of 1998	Empowers the FTC to set rules regarding how and when marketers must obtain parental permission before asking children marketing research questions.
Aviation Security Act of 2001	Requires airlines to take extra security measures to protect passengers, including the installation of stronger cockpit doors, improved baggage screening, and increased security training for airport personnel.
Homeland Security Act of 2002	Protects consumers against terrorist acts. Created the Department of Homeland Security.
Do Not Call Law of 2003	Protects consumers against unwanted telemarketing calls.
CAN-SPAM Act of 2003	Protects consumers against unwanted e-mail, or spam.

marketing affairs. These agencies, plus others, are discussed throughout the book, but a brief introduction is in order at this point.

Consumer Product Safety Commission (CPSC)
A federal agency established to protect the health and safety of consumers in and around their homes.

Federal Trade Commission (FTC)
A federal agency empowered to prevent persons or corporations from using unfair methods of competition in commerce.

The sole purpose of the Consumer Product Safety Commission (CPSC) is to protect the health and safety of consumers in and around their homes. The CPSC has the power to set mandatory safety standards for almost all products that consumers use (about 15,000 items). The CPSC consists of a five-member committee and about 400 staff members, including technicians, lawyers, and administrative help. The commission can fine offending firms up to $500,000 and sentence their officers to up to a year in prison. It can also ban dangerous products from the marketplace. The CPSC oversees about 400 recalls per year. The CPSC operates under rules that prohibit staff from publicizing information about product complaints until the manufacturer OK's the release. Besides handing over a lot of control to companies, this process routinely delays public disclosure of hazards. It has also been suggested that the CPSC is extremely underfunded.[72]

The Federal Trade Commission (FTC) also consists of five members, each holding office for seven years. The FTC is empowered to prevent persons or corporations from using unfair methods of competition in commerce. It is authorized to investigate the practices of business combinations and to conduct hearings on

Exhibit 4.6

Powers of the Federal Trade Commission

REMEDY	PROCEDURE
Cease-and-Desist Order	A final order is issued to cease an illegal practice—and is often challenged in the courts.
Consent Decree	A business consents to stop the questionable practice without admitting its illegality.
Affirmative Disclosure	An advertiser is required to provide additional information about products in advertisements.
Corrective Advertising	An advertiser is required to correct the past effects of misleading advertising. (For example, 25 percent of a firm's media budget must be spent on FTC-approved advertisements or FTC-specified advertising.)
Restitution	Refunds are required to be given to consumers misled by deceptive advertising. According to a 1975 court-of-appeals decision, this remedy cannot be used except for practices carried out after the issuance of a cease-and-desist order.
Counteradvertising	The FTC proposed that the Federal Communications Commission permit advertisements in broadcast media to counteract advertising claims (also that free time be provided under certain conditions).

antitrust matters and deceptive advertising. The FTC has a vast array of regulatory powers (see Exhibit 4.6). Nevertheless, it is not invincible. For example, the FTC had proposed to ban all advertising to children under age 8, to ban all advertising of the sugared products that are most likely to cause tooth decay to children under age 12, and to require the food industry to pay for dental health and nutritional advertisements. Business reacted by lobbying to reduce the FTC's power. The two-year lobbying effort resulted in passage of the FTC Improvement Act of 1980. The major provisions of the act are as follows:

> It bans the use of unfairness as a standard for industry-wide rules against advertising. All the proposals concerning children's advertising were therefore suspended, because they were based almost entirely on the unfairness standard. It requires oversight hearings on the FTC every six months. This congressional review is designed to keep the commission accountable. Moreover, it keeps Congress aware of one of the many regulatory agencies it has created and is responsible for monitoring.

Businesses rarely band together to create change in the legal environment as they did to pass the FTC Improvement Act. Generally, marketing managers react only to legislation, regulation, and edicts. It is usually less costly to stay attuned to the regulatory environment than to fight the government. If marketers had toned down their hard-hitting advertisements to children, they might have avoided an FTC inquiry altogether. The FTC also regulates advertising on the Internet as well as Internet abuses of consumer privacy (discussed in Chapter 9). The Food and Drug Administration (FDA), another powerful agency, is charged with enforcing regulations against selling and distributing adulterated, misbranded, or hazardous food and drug products. In the last decade it took a very aggressive stance against tobacco products and is now paying attention to the fast-food industry.

Food and Drug Administration (FDA)
A federal agency charged with enforcing regulations against selling and distributing adulterated, misbranded, or hazardous food and drug products.

THE BATTLE OVER CONSUMER PRIVACY

The popularity of the Internet for direct marketing, for collecting consumer data, and as a repository for sensitive consumer data has alarmed privacy-minded consumers. So many online users have complained about "spam," the Internet's equivalent of junk mail, that the U.S. Congress passed the CAN-SPAM Act in an attempt to regulate it. The act, which took effect on January 1, 2004, does not ban spam, but it does prohibit commercial e-mailers from using a false address and presenting false or misleading information. It also requires commercial e-mailers to provide a way for recipients to "opt out" of receiving further e-mail from the sender.

Another problem is that Web surfers, including children who are using the Internet, are routinely asked to divulge personal information in order to access certain screens or purchase goods or services online. Internet users who once felt fairly anonymous when using the Web are now disturbed by the amount of information marketers collect on them and their children as they visit various sites in cyberspace.

Most consumers are unaware of how technology is used to collect personal data or how the personal information is used and distributed after it is collected. The government actively sells huge amounts of personal information to list compilers. State motor vehicle bureaus sell names and addresses of individuals who get driver's licenses. Hospitals sell the names of women who just gave birth on their premises. Consumer credit databases, developed and maintained by large providers such as Equifax Marketing Services and TransUnion, are often used by credit card marketers to prescreen targets for solicitations.

While privacy policies for companies in the United States are largely voluntary and there are almost no regulations on the collection and use of personal data, collecting consumer data outside the United States is a different matter. Database marketers venturing into new data territories must carefully navigate foreign privacy laws. The European Union's *European Data Protection Directive,* for instance, states that any business that trades with a European organization must comply with the EU's rules for handling information about individuals or risk prosecution. This directive prohibits the export of personal data to countries not doing enough to protect privacy, in particular, the United States.

More than 50 nations have, or are developing, privacy legislation. Europe has the strictest legislation regarding the collection and use of consumer data, and other countries look to that legislation when formulating their policies. Australia, for instance, recently introduced legislation that would require private companies to follow a set of guidelines regarding the collection, storage, use, and transfer of personal information about individuals. Common privacy rules include obtaining data fairly and lawfully, using the information only for the original purpose specified, making sure it is accurate and up-to-date, and destroying data after the purpose for collection is completed. The EU requires that consumers be presented with an opt-out provision at the point of data collection.

Despite cries from consumer and advocacy groups for privacy legislation, to date Congress has failed to act. So far, only the states have enacted meaningful protections, with California in the lead. Now, more than 30 states have adopted laws that require notification if a customer's personal information has been improperly exposed. In 2007, The TJX Companies, which owns Marshalls, T.J. Maxx, Home Goods, and A.J. Wright, reported that customers' credit and debit card information, along with some driver's license data had been lifted from its computer system. When asked how many people were affected, a spokesperson for TJX replied, "substantially less than millions."[73] Others put the number of persons exposed at 45 million.[74]

Identity Theft

People are right to be concerned about their personal information. Identity theft costs $55 billion per year. One company that has come under fire is ChoicePoint. Since spinning off from the credit bureau Equifax in 1997, it has been buying up databases and data-mining operations. Businesses, individuals, and even the FBI now rely on its storehouse. But its customers have also included Nigerian scammers who apparently used the data to steal people's identities.

In 1998, Congress passed the Identity Theft and Assumption Deterrence Act. This law prohibits knowingly transferring or using another person's identification with the intent to commit an unlawful activity, e.g., theft of funds. Guilty parties face up to 15 years in prison.

Governmental Actions

Three other key laws (one a state law) have been passed to protect consumers from identity theft. The federal laws are:

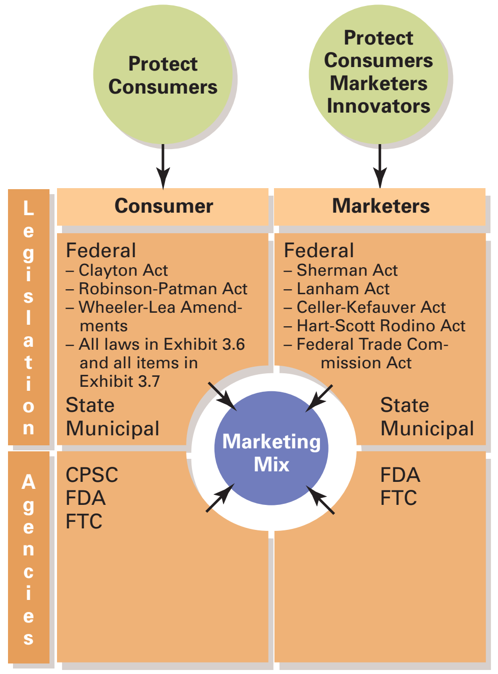
- *Gramm-Leach-Bliley Act (Financial Services Modernization Act)*: This act is aimed at financial companies. It requires those corporations to tell their customers how they use their personal information and to have policies that prevent fraudulent access to it. Partial compliance has been required since 2001.
- *Health Insurance Portability and Accountability Act*: This law is aimed at the healthcare industry. It limits disclosure of individuals' medical information and imposes penalties on organizations that violate privacy rules. Compliance has been required for large companies since 2003.

The state law is:

- *California's Notice of Security Breach Law*: If any company or agency that has collected personal information about a California resident discovers that nonencrypted information has been taken by an unauthorized person, the company or agency must tell the resident. Compliance has been required since 2003. (Some 30 other states are considering similar laws.)

REVIEW LEARNING OUTCOME

LO7 Discuss the political and legal environment of marketing



LO8 Competitive Factors

The competitive environment encompasses the number of competitors a firm must face, the relative size of the competitors, and the degree of interdependence within the industry. Management has little control over the competitive environment confronting a firm.

COMPETITION FOR MARKET SHARE AND PROFITS

As U.S. population growth slows, global competition increases, costs rise, and available resources tighten, firms find that they must work harder to maintain their profits and market share regardless of the form of the competitive market. Take, for example, the competition among airlines. In the aftermath of September 11, 2001, the airline industry imploded. Proud competitors, including United Airlines, Delta Air Lines, and Northwest Airlines, declared bankruptcy as rising fuel prices added to their woes. American Airlines, the world's largest airline, teetered on the brink of going under. Survival in such a horrific environment meant drastically cutting costs and squeezing out revenue wherever possible. Yet one competitor not only survived, but managed to earn a profit. Southwest Airlines made money and avoided layoffs with its efficient strategy based on one type of plane and lower labor costs.

The airlines' problems have made the competitive environment more challenging for firms in the commercial aircraft industry. American aircraft manufacturer

© PR NEWSFOTO/DYSON

Boeing still faces competition from European company Airbus, even though Airbus recently lost its edge in that $50 billion market. In 2006, Airbus was beset with problems, while Boeing's new 787 Dreamliner gave the company a much needed lift. Marketers tout the Dreamliner's features, which include large windows, mood lighting, electronic shades, wider seats and aisles, and a state-of-the-art climate control system, as providing a unique flying experience. By 2007, Boeing had sold over 500 Dreamliners, whereas the huge Airbus A350 lagged far behind.

Boeing's idea is to include an outreach to passengers, along with spreadsheets and fuel consumption data, in its sales pitch to airline executives. Just as Intel created a desire for personal computers containing its microchips and Nokia used its unique cell phone features to drive demand among Verizon and Cingular customers, Boeing intends to create further demand for the 787s by including postsale service that highlights to passengers the benefits the planes provide and that are consistent with the carrier's brand. "The more people fly, the more they develop a preference for the type of aircraft they fly in," asserts Robert Pollack, Boeing's vice president for brand and marketing positioning. "A lot more can be done to suggest to consumers that the airline they fly in the future can make a difference in their air travel."[75]

GLOBAL COMPETITION

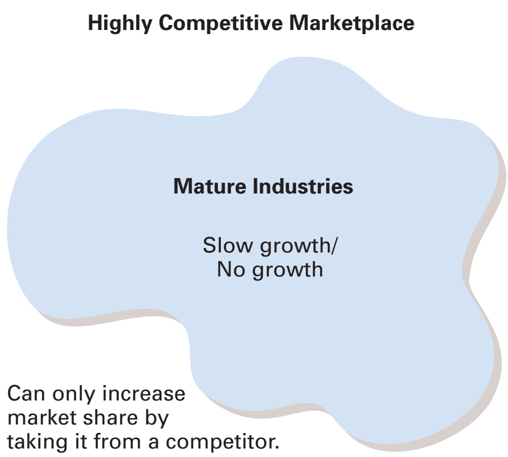
Boeing, is a very savvy international competitor conducting business throughout the world. Many foreign competitors also consider the United States to be a ripe target market. Thus, a U.S. marketing manager can no longer focus only on domestic competitors. In automobiles, textiles, watches, televisions, steel, and many other areas, foreign competition has been strong. In the past, foreign firms penetrated U.S. markets by concentrating on price, but today the emphasis has switched to product quality. Nestlé, Sony, Rolls-Royce, and Sandoz Pharmaceuticals are noted for quality, not cheap prices.

For a century, vacuuming has been synonymous with one brand, whose iconic status is such that the British and French still refer to "hoovering the carpet." But two years after launching his bagless cleaners in the United States, English inventor James Dyson's company now makes America's best-selling vacuum. Dyson has captured 21 percent of the U.S. market, leaving Canton, Ohio–based Hoover with 16 percent. Dyson's clean sweep is all the more surprising given that his product goes for $399 to $550 while an average vacuum costs $150.[76]

Global competition is discussed in much more detail in Chapter 5.

REVIEW LEARNING OUTCOME

LO8 Explain the basics of foreign and domestic competition



6 < components of the external marketing environment

$21 < billion spent by tweens in 2008

percent of adult Americans who get less than 7 hours of sleep each night > **40**

56,000 < drivers at UPS

maximum fine CPSC can issue for violations > **$500,000**

Review and Applications

LO 1 **Discuss the external environment of marketing and explain how it affects a firm.** The external marketing environment consists of social, demographic, economic, technological, political and legal, and competitive variables. Marketers generally cannot control the elements of the external environment. Instead, they must understand how the external environment is changing and the impact of that change on the target market. Then marketing managers can create a marketing mix to effectively meet the needs of target customers.

1.1 What is the purpose of environmental scanning? Give an example.

TEAM

1.2 Form six teams and make each one responsible for one of the uncontrollable elements in the marketing environment. Your boss, the company president, has asked each team to provide one-year and five-year forecasts of the major trends the firm will face. The firm is in the telecommunications equipment industry. It has no plans to become a telecommunications service provider like, for example, Verizon and AT&T. Each team should use the library, the Internet, and other data sources to make its forecasts. Each team member should examine a minimum of one data source. The team members should then pool their data and prepare a recommendation. A spokesperson for each team should present the findings to the class.

LO 2 **Describe the social factors that affect marketing.** Within the external environment, social factors are perhaps the most difficult for marketers to anticipate. Several major social trends are currently shaping marketing strategies. First, people of all ages have a broader range of interests, defying traditional consumer profiles. Second, changing gender roles are bringing more women into the workforce and increasing the number of men who shop. Third, an increase in the number of dual-career families has created demand for time-saving goods and services.

2.1 Every country has a set of core values and beliefs. These values may vary somewhat from region to region of the nation. Identify five core values for your area of the country. Clip magazine advertisements that reflect these values and bring them to class.

2.2 Give an example of component lifestyles based on someone you know.

LO 3 **Explain the importance to marketing managers of current demographic trends.** Today, several basic demographic patterns are influencing marketing mixes. Because the U.S. population is growing at a slower rate, marketers can no longer rely on profits from generally expanding markets. Marketers are also faced with increasingly experienced consumers among the younger generations such as tweens and teens. And because the population is also growing older, marketers are offering more products that appeal to middle-aged and older consumers.

3.1 Baby boomers in America are aging. Describe how this might affect the marketing mix for the following:

a. Bally's Health Clubs

b. McDonald's

c. Whirlpool Corporation

d. The state of Florida

e. Target stores

WRITING

3.2 You have been asked to address a local Chamber of Commerce on the subject of "Generation Y." Prepare an outline for your talk.

3.3 How should Ford Motor Company market differently to Generation Y, Generation X, and baby boomers?

LO 4 **Explain the importance to marketing managers of multiculturalism and growing ethnic markets.** Multiculturalism occurs when all major ethnic groups in an area are roughly equally represented. Growing multiculturalism makes the marketer's task more challenging. America is not a melting pot but numerous mini-melting pots. Hispanics are the fastest-growing segment of the population followed by African Americans. Many companies are now creating departments and product lines to effectively target multicultural market segments. Companies have quickly found that ethnic markets are not homogeneous.

4.1 Go to the library and look up a minority market such as the Hispanic market. Write a memo to your boss that details the many submarkets within this segment.

ONLINE

4.2 Using the library and the Internet, find examples of large companies directing marketing mixes to each major ethnic group.

LO5

Identify consumer and marketer reactions to the state of the economy. In recent years, U.S. incomes have risen at a slow pace. At the same time, the financial power of women has increased, and they are making the purchasing decisions for many products in traditionally male-dominated areas. During a time of inflation, marketers generally attempt to maintain level pricing to avoid losing customer brand loyalty. During times of recession, many marketers maintain or reduce prices to counter the effects of decreased demand; they also concentrate on increasing production efficiency and improving customer service.

5.1 Explain how consumers' buying habits may change during a recessionary period.

WRITING

5.2 Periods of inflation require firms to alter their marketing mix. Suppose a recent economic forecast predicts that inflation will be almost 10 percent during the next 18 months. Your company manufactures hand tools for the home gardener. Write a memo to the company president explaining how the firm may have to alter its marketing mix.

LO6

Identify the impact of technology on a firm. Monitoring new technology is essential to keeping up with competitors in today's marketing environment. The United States excels in basic research and, in recent years, has dramatically improved its track record in applied research. Without innovation, U.S. companies can't compete in global markets. Innovation is increasingly becoming a global process.

6.1 Give three examples of how technology has benefited marketers. Also, give several examples of firms that have been hurt because they did not keep up with technological changes.

LO7

Discuss the political and legal environment of marketing. All marketing activities are subject to state and federal laws and the rulings of regulatory agencies. Marketers are responsible for remaining aware of and abiding by such regulations. Some key federal laws that affect marketing are the Sherman Act, Clayton Act, Federal Trade Commission Act, Robinson-Patman Act, Wheeler-Lea Amendments to the FTC Act, Lanham Act, Celler-Kefauver Antimerger Act, and Hart-Scott-Rodino Act. Many laws, including privacy laws, have been passed to protect the consumer as well. The Consumer Product Safety Commission, the Federal Trade Commission, and the Food and Drug Administration are the three federal agencies most involved in regulating marketing activities.

7.1 The Federal Trade Commission and other governmental agencies have been both praised and criticized for their regulation of marketing activities. To what degree do you think the government should regulate marketing? Explain your position.

7.2 Can you think of any other areas where consumer protection laws are needed?

ONLINE

7.3 What topics are currently receiving attention in FDA News (**http://www.fdanews.com**)? What effect has the attention had on market share?

LO8

Explain the basics of foreign and domestic competition. The competitive environment encompasses the number of competitors a firm must face, the relative size of the competitors, and the degree of interdependence within the industry. Declining population growth, rising costs, and shortages of resources have heightened domestic competition.

8.1 Explain how the nature of competition is changing in America.

8.2 Might there be times when a company becomes too competitive? If so, what could be the consequences?

Key Terms

Exercises

TEAM

APPLICATION EXERCISE

The importance of cultural understanding cannot be overstated, especially in today's global marketplace and our own multicultural country. In general, Americans tend to be ethnocentric; that is, they are quick to prejudge other cultural norms as wrong (or of less significance) because they differ from American practices.

One way to be exposed to another culture is by examining the foods typical of that culture. In this exercise, you will need to work in a team to create a guide to ethnic dining in your city or area. The finished guide will be descriptive in nature; it is not meant to be a rating guide.[77]

Activities

1. Identify ethnic dining categories for inclusion in your guide. Once you have identified categories for your area, make a list of restaurants for each category.
2. You will need to create a data collection form so that the same information is collected from each restaurant. For example, you will want to include the name, address, and phone number for each restaurant. Think of other information that would be helpful.
3. Divide up the restaurant list your team generated in activity 1 so that each team member is responsible for collecting information from a certain number of restaurants. Consider dividing the list geographically so that each team member can visit an assortment of ethnic restaurants. If your budget allows, eat at a few of the restaurants in addition to collecting the information. After you have all the information, meet to review and compare your findings.
4. Was there a meal or type of food that you particularly liked? Disliked? Which type of ethnic restaurant seemed most foreign to you? Why do you think that was?

ETHICS

ETHICS EXERCISE

Gary Caplan has developed a new "energy drink" designed to burn calories while sleeping, which he intends to market to grossly overweight consumers. According the Center for Disease Control and Prevention, 20 percent of Americans are obese. Gary's mother, a doctor, argues that it's unethical to target the obese–that they are as vulnerable a target market as the elderly and children.

Questions

1. Is Gary targeting a "vulnerable" market?
2. Does the AMA Statement of Ethics address this issue? Go to http://www.marketingpower.com and review the statement. Then write a brief paragraph on what it contains that relates to Gary Caplan's marketing decision.

© AP PHOTO/ELIZABETH DALZIEL

Case Study: Starbucks

SELLING COFFEE IN THE LAND OF TEA[78]

Starbucks has been doing business in China since 1999 when they opened their first coffee shop in Beijing. Today hundreds of Starbucks stores sell coffee in the land of tea, including one at the Great Wall. It has become one of the most popular brands among the country's 20-to-40-year-old upwardly mobile Chinese, or "Chuppies," as they're called, but so far China only accounts for about 10 percent of Starbucks' global sales. Nevertheless, Chairman Howard Schultz believes the country will someday be the company's largest market outside North America. "The market response," he says, "has exceeded our expectations."

This may seem surprising when you consider the fact that the majority of China's one billion-plus population are tea drinkers who didn't know what coffee was until Nestle introduced a powdered version on store shelves in the 1980s. But Starbucks is betting that they can win the new generation over by marketing its signature product as an emblem of modern China's new sophistication.

"Coffee represents the change," says Wang Jinlong, president of Starbucks Greater China. "The disposable income is concentrated on the young people, and this is the place they want to come." Success in China could depend on how well Starbucks markets itself to what Wang calls the "little emperors." China's one-child law has spawned a generation that isn't interested in collective goals, he says. Instead, they embrace the Western belief in individuality that Starbucks embodies.

After surveying Chinese consumers, Starbucks compiled a list of the top reasons they go to cafés. Surprisingly, the number-one reason was "to gather with family and friends," while "to drink coffee" lagged behind at number six. Living spaces are generally small and cramped there, making places to congregate important to the Chinese.

Da Wei Sun, manager of outlets in Beijing, believes that Starbucks found success in China because they took this idea of a place to gather and gave people in the cities a "third space" beyond work and home, making it cool to have a latte and hang out. Starbucks offers more food on the Chinese menu, including duck sandwiches, moon pies, and green-tea cheesecake, than in other countries, and more seating as well. Only 20 percent of North American customers eat and drink inside the store after ordering, but the number is close to 90 percent in China.

China remains a communist country, so a change in its one-party dictatorship could potentially affect business overnight. Schultz says the key to establishing stores there is to first find local partners who understand the changing political and business landscapes. Starbucks initially entered China by authorizing local developers to use their brand and setting up joint ventures with partners.

Industry analyst Pei Liang advised that for long-term success in the country, Starbucks would need to acquire controlling stakes in its joint ventures. This, Liang explained, would strengthen management's control and put them in position to reap more of the profits as the market grew. "Licensing or holding a minority stake is an effective tool when first stepping into a new market because it involves a small investment," says Liang. "But Starbucks, the brand's owner, only receives royalty fees from the licensee."

In late 2006, Starbucks announced that it was buying out its partner in China and taking control of 60 stores. The market had changed after Beijing entered the World Trade Organization in 2001, making it easier for foreign companies to navigate alone. "Buying out one's partner is becoming more common," says industry consultant Kent D. Kedl. "Starbucks probably feels they know better how China works now so they can go it on their own."

Chairman Howard Schultz says that Starbucks will concentrate most of its future expansion efforts in China, and Kedl predicts they will see continued success there: "It's not just a drink in China. It's a destination. It's a place to be seen and a place to show how modern one is." And with China's economy continuing to grow in double digits, the number of Chuppies willing to pay $3.63 for a Mocha Frappuccino Grande is likely to grow, too.

Questions

1. Many of the same environmental factors, such as cultural factors, that operate in the domestic market also exist internationally. Discuss the key cultural factors Starbucks had to consider as it expanded into China.
2. Discuss the key political and legal factors Starbucks had to consider in the Chinese marketplace. What are the risks of entering a country with these factors? What changes have occurred in China's political and legal structure to the advantage of foreign companies?
3. What demographic factors were important for Starbucks to understand in China? What were the demographics they decided to target?

4. What was the initial global-market strategy Starbucks employed to enter China? Discuss the advantages and disadvantages to this early strategy. How has their strategy changed since then and why?

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Company Clips

METHOD – ENTERING A CROWDED MARKET

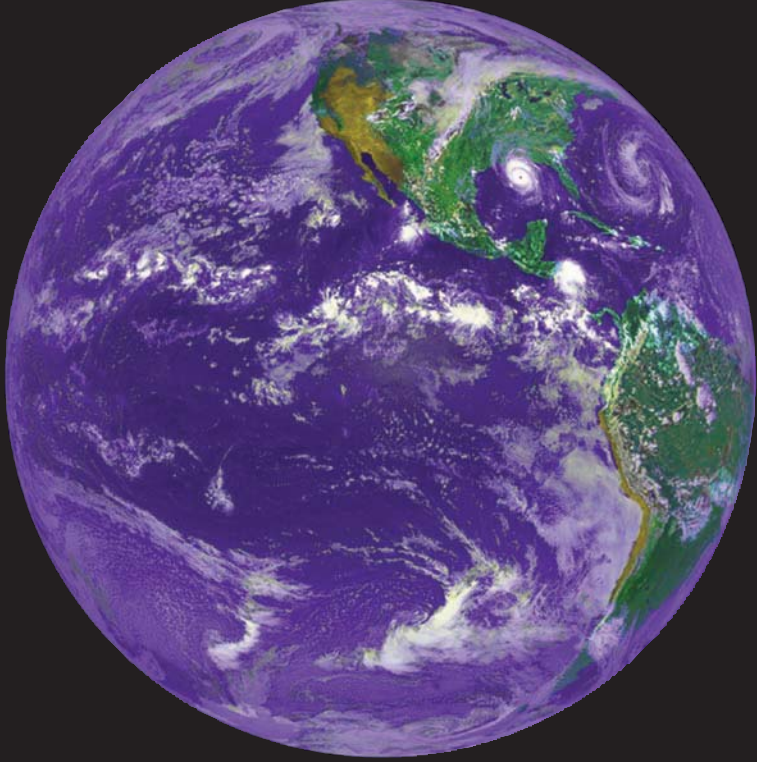
Companies large and small, new and old are all participants in the market, and as such, they are all subject to the forces that act on each entity in the marketplace. The same is true of method. As you've already seen in the Company Clips from chapters 2 & 3, method has been attentive to the customer, analyzed the competition, focused on social change, and identified economic factors that have affected how it does and will do business. Review the Company Clips from chapters 2 and 3 to hear founders Adam Lowry and Eric Ryan and CEO Alastair Dorward describe several factors in the external environment that have influenced how method entered the market and the success the company has experienced.

Questions

1. method's founders and CEO repeatedly reference the role of competition and consumers in their assessments of their external environment. Is there a hierarchy to the environmental factors discussed in this chapter? Explain.
2. Should other companies imitate the emphasis method gives to certain factors in its external environment? Why or why not?
3. Does method's assessment of its external environment seem to be lacking anything? What?

Marketing & You Results

A high score means you have a strong perception of time limitations for work-related task completion. Research indicates that when you perceive yourself to be working under time pressure, your creativity is negatively affected. As you read in Chapter 4, time is an important social factor in the external environment that affects marketing. Understanding your own perceptions and reaction to time constraints will be helpful in planning to meet the needs of the time-constrained consumer. Your challenge as a busy marketer will be to continue thinking creatively on their behalf.



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CHAPTER 5

Developing a Global Vision

Learning Outcomes

- LO 1 Discuss the importance of global marketing
- LO 2 Discuss the impact of multinational firms on the world economy
- LO 3 Describe the external environment facing global marketers
- LO 4 Identify the various ways of entering the global marketplace
- LO 5 List the basic elements involved in developing a global marketing mix
- LO 6 Discover how the Internet is affecting global marketing

LO 1

Rewards of Global Marketing

global marketing
Individuals and organizations using a global vision to effectively market goods and services across national boundries.

global vision
Recognizing and reacting to international marketing opportunities, using effective global marketing strategies, and being aware of threats from foreign competitors in all markets.

Today, global revolutions are under way in many areas of our lives such as management, politics, communications, and technology. The word *global* has assumed a new meaning, referring to a boundless mobility and competition in social, business, and intellectual arenas. No longer just an option, global marketing—individuals and organizations using a global vision to effectively market goods and services across national boundaries—has become imperative for business.

U.S. managers must develop a global vision not only to recognize and react to international marketing opportunities but also to remain competitive at home. Often a U.S. firm's toughest domestic competition comes from foreign companies. Moreover, a global vision enables a manager to understand that customer and distribution networks operate worldwide, blurring geographic and political barriers and making them increasingly irrelevant to business decisions. In summary, having a global vision means recognizing and reacting to international marketing opportunities, using effective global marketing strategies, and being aware of threats from foreign competitors in all markets.

Over the past two decades, global trade has climbed from $200 billion a year to over $11 trillion. Countries and companies that were never considered major players in global marketing are now important, and some of them show great skill.

Today, marketers face many challenges to their customary practices. Product development costs are rising, the life of products is getting shorter, and new technology is spreading around the world faster than ever. But marketing winners relish the pace of change instead of fearing it.

An example of a young company with a global vision that has capitalized on new technology is Ashtech in Sunnyvale, California. Ashtech makes equipment to capture and convert satellite signals from the U.S. government's Global Positioning System. Ashtech's chief engineer and his team of ten torture and test everything built by Ashtech—expensive black boxes of chips and circuits that use satellite signals to tell surveyors, farmers, mining machine operators, and others where they are with great accuracy. Over half of Ashtech's output is exported. Its biggest customer is Japan.

Adopting a global vision can be very lucrative for a company. Gillette, for example, gets about two-thirds of its revenue from its international division. H. J. Heinz, the ketchup company, gets over half of its revenue from international sales. Although Cheetos and Ruffles haven't done very well in Japan, the potato chip has been quite successful. PepsiCo's (owner of Frito-Lay) overseas snack business brings in more than $3.25 billion annually. The William Wrigley Jr. Company, makers of Wrigley's Spearmint, Juicy Fruit, Altoids, Life Savers, and other products, has global annual sales of over $4.7 billion.[1]

Marketing & You

How would you describe your interest in other cultures? Enter your answers on the lines provided.

1	2	3	4	5	6	7
Strongly disagree			Neither disagree nor agree			Strongly agree

— I would like to have opportunities to meet people from other countries.

— I am very interested in trying food from different countries.

— We should have a respect for traditions, cultures, and ways of life of other nations.

— I would like to learn more about other countries.

— I have a strong desire for overseas travel.

— I would like to know more about foreign cultures and customs.

— I have a strong desire to meet and interact with people from foreign countries.

Now, total your score. Read the chapter, and find out what your score means at the end.

From Scale #98, Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds. Vol. III © by American Marketing Association.

Another company with a global vision is Pillsbury. The Pillsbury Doughboy is used in India to sell a product that the company had just about abandoned in America: flour. Pillsbury (owned by General Mills) has many higher-margin products such as microwave pizzas in other parts of the world, but it discovered that in this tradition-bound market, it needed to push the basics.

Even so, selling packaged flour in India has been almost revolutionary, because most Indian housewives still buy raw wheat in bulk, clean it by hand, store it in huge metal hampers, and, every week, carry some to a neighborhood mill, or *chakki*, where it is ground between two stones.

To help reach those housewives, the Doughboy himself has gotten a makeover. In TV advertising, he presses his palms together and bows in the traditional Indian greeting. He speaks six regional languages.

Global marketing is not a one-way street, whereby only U.S. companies sell their wares and services throughout the world. Foreign competition in the domestic market used to be relatively rare but now is found in almost every industry. In fact, in many industries U.S. businesses have lost significant market share to imported products. In electronics, cameras, automobiles, fine china, tractors, leather goods, and a host of other consumer and industrial products, U.S. companies have struggled at home to maintain their market shares against foreign competitors. In 2007, Toyota became the number one automobile company in the American market.

IMPORTANCE OF GLOBAL MARKETING TO THE UNITED STATES

Many countries depend more on international commerce than the United States does. For example, France, Britain, and Germany all derive more than 19 percent of their gross domestic product (GDP) from world trade, compared to about 12 percent for the United States. Nevertheless, the impact of international business on the U.S. economy is still impressive:

- The United States exports about a fifth of its industrial production.
- One in every five jobs in the United States is directly or indirectly supported by exports.[2]
- Every U.S. state has realized net employment gains directly attributed to foreign trade.[3]
- U.S. businesses export over $800 billion in goods to foreign countries every year, and almost a third of U.S. corporate profits comes from international trade and foreign investment.
- Exports account for 25 percent of U.S. economic growth.
- The United States is the world's leading exporter of farm products, selling more than $60 billion in agricultural exports to foreign countries each year.
- Chemicals, office machinery and computers, automobiles, aircraft, and electrical and industrial machinery make up almost half of all nonagricultural exports.
- About half of U.S. merchandise imports are raw materials, capital goods, and industrial products used by U.S. manufacturers to make goods in the United States.[4] America is the world's largest importer.

These statistics might seem to imply that practically every business in the United States is selling its wares throughout the world, but nothing could be further from the truth. About 85 percent of all U.S. exports of manufactured goods are shipped by 250 companies; less than 10 percent of all manufacturing businesses, or around 25,000 companies, export their goods on a regular basis. Most small- and medium-sized firms are essentially nonparticipants in global trade and marketing. Only the very

© AP PHOTO

large multinational companies have seriously attempted to compete worldwide. Fortunately, more of the smaller companies are now aggressively pursuing international markets.

THE FEAR OF TRADE AND GLOBALIZATION

The protests during meetings of the World Trade Organization, the World Bank, and the International Monetary Fund (the three organizations are discussed later in the chapter) show that many people fear world trade and globalization. What do they fear? The negatives of global trade are as follows:

- Millions of Americans have lost jobs due to imports, production shifts abroad, or outsourcing of tech jobs. Most find new jobs—often for lower pay.
- Millions of others fear losing their jobs, especially at those companies operating under competitive pressure.
- Employers often threaten to outsource jobs if workers do not accept pay cuts.
- Service and white-collar jobs are increasingly vulnerable to operations moving offshore.

Jobs Outsourcing The notion of *jobs outsourcing* (sending U.S. jobs abroad) has been highly controversial for the past several years. Many executives say that it is about corporate growth, efficiency, productivity and revenue growth. Most companies see cost savings as a key driver in outsourcing. One survey of large U.S. companies found that 91 percent said "labor costs" were an "important" or "very important" factor in their decision to offshore work.[5] Eric Rongley, CEO of Bleum, Inc., a Shanghai-based software outsourcing company, claims that, "Over the next ten years the outsourcing market will grow over 900 percent."[6] While India, because of its educated, English-speaking population, has always been a popular country for receiving offshoring work, other countries are gaining as well. Exhibit 5.1 shows types of offshore work by location. The survey respondents were 531 multinational firms located in the United States and Europe.[7]

Exhibit 5.1

Types of Offshore Work by Location (Percentage of 531 firms citing location by function)

	Administrative	Contact Centers	IT	Procurement	Product Development
China	16	5	17	21	41
India	28	13	31	5	24
Philippines	35	35	16	8	6
Other Asia	30	17	30	3	20
Eastern Europe	23	13	31	8	26
Western Europe	27	15	27	6	24
Canada	22	39	22	0	17
Latin America	22	24	22	9	22
Mexico	22	22	33	11	11

SOURCE: Duke University/Booz Allen Offshoring Research Network 2006 Survey

While many corporations are excited about the advantages of offshoring, politicians, unions, and workers are not. Alan Blinder, former Federal Reserve Vice-Chairman, says as many as 40 million jobs may be shipped out of the country in the next decade or two.[8] That is more than double the total of workers employed in manufacturing today. Dr. Blinder notes that new communications technology allows services to be delivered electronically from afar. His list of "highly offshorable jobs" are:

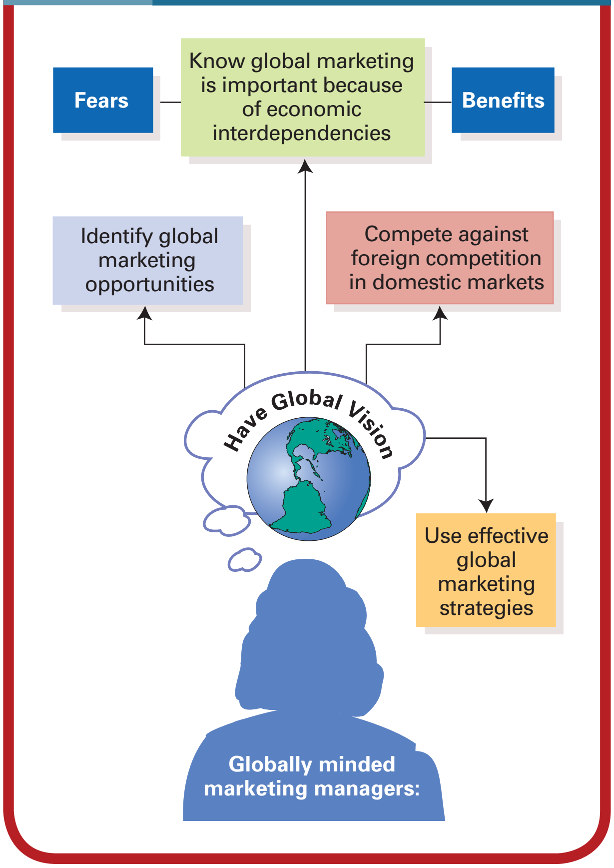
Occupation	Number of U.S. workers[9]
Computer programmers	389,090
Data entry keyers	296,700
Actuaries	15,770
Film and video editors	15,200
Mathematicians	2,930
Medical transcriptionists	90,380
Interpreters and translators	21,930
Economists	12,490
Graphic designers	178,530
Bookkeeping, accounting and auditing clerks	1,815,340
Microbiologists	15,250
Financial analysts	180,910

Other economists strongly disagree with Dr. Blinder. Dr. Jagdish Bhagwati, Columbia University, says, "He's dead wrong. I have no doubt that we are creating far more jobs than we are losing."[10]

BENEFITS OF GLOBALIZATION

REVIEW LEARNING OUTCOME

LO 1 Discuss the importance of global marketing



Traditional economic theory says that globalization relies on competition to drive down prices and increase product and service quality. Business goes to the countries that operate most efficiently and/or have the technology to produce what is needed.

In summary, globalization expands economic freedom, spurs competition, and raises the productivity and living standards of people in countries that open themselves to the global marketplace. For less developed countries, globalization also offers access to foreign capital, global export markets, and advanced technology while breaking the monopoly of inefficient and protected domestic producers. Faster growth, in turn, reduces poverty, encourages democratization, and promotes higher labor and environmental standards. Though government officials may face more difficult choices as a result of globalization, their citizens enjoy greater individual freedom. In this sense, globalization acts as a check on governmental power by making it more difficult for governments to abuse the freedom and property of their citizens.

Globalization deserves credit for helping lift many millions out of poverty and for improving standards of living for low-wage families. In developing countries around the world, globalization has created a vibrant middle class that has elevated the standards of living for hundreds of millions of people. That's particularly true in China, where the incomes of low-skilled workers have consistently risen. The poor in countries like Vietnam and elsewhere in Southeast Asia have also benefited greatly since those countries have opened their economies. In many developing countries around the world, life expectancies and health care have improved, as have educational opportunities.[11]

LO 2
Multinational Firms

multinational corporation
A company that is heavily engaged in international trade, beyond exporting and importing.

The United States has a number of large companies that are global marketers. Many of them have been very successful. A company that is heavily engaged in international trade, beyond exporting and importing, is called a **multinational corporation.** Multinational corporations move resources, goods, services, and skills across national boundaries without regard to the country in which the headquarters are located. The world's leading multinational firms are listed in Exhibit 5.2. In 2006, to be ranked as one of the 500 largest multinationals, a firm needed revenue of $12.6 billion. That is more than the GDP of Jordan or Jamaica.[12] These organizations are as big as small countries! Indeed, Wal-Mart's annual sales are larger than the GDP of all but 30 nations in the world.

Multinationals often develop their global business in stages. In the first stage, companies operate in one country and sell into others. Second-stage multinationals set up foreign subsidiaries to handle sales in one country. In the third stage, they operate an entire line of business in another country. The fourth stage has evolved primarily due to the Internet and involves mostly high-tech companies. For these firms, the executive suite is virtual. Their top executives and core corporate functions are in different countries, wherever the firms can gain a competitive edge through the availability of talent or capital, low costs, or proximity to their most important customers.

A good example of a fourth-stage company is Trend Micro, an Internet antivirus software company.[13] Its top executives, engineers, and support staff are spread around the world so that they can respond quickly to new virus threats—which can start anywhere and spread like wildfire. The main virus response center is in the Philippines, where 250 ever-vigilant engineers work evening and midnight shifts as needed. Six other labs are scattered from Munich to Tokyo.

Trend Micro's financial headquarters is in Tokyo, where it went public; product development is in Ph.D.-rich Taiwan; and most of its sales are in Silicon Valley—inside the giant American market. When companies fragment this way, they are no longer limited to the strengths, or hobbled by the weaknesses, of their native lands.

Such fourth-stage multinationals are being created around the world. They include business-intelligence-software maker Business Objects, with headquarters in France and San Jose, California; Wipro, a tech-services supplier with headquarters in India and Santa Clara, California; and computer-peripherals maker Logitech International, with headquarters in Switzerland and Fremont, California.

Exhibit 5.2

The World's Largest Multinational Corporations

Rank	Company	Country	Revenues ($ millions)
1	Wal-Mart Stores	U.S.	351,139.0
2	ExxonMobil	U.S.	347,254.0
3	Royal Dutch/Shell	Netherlands	318,845.0
4	BP	Britain	274,316.0
5	General Motors	U.S.	207,349.0
6	Toyota Motor	Japan	204,746.4
7	Chevron	U.S.	200,567.0
8	DaimlerChrysler	Germany	190,191.4
9	ConocoPhillips	U.S.	172,451.0
10	Total	France	168,356.7
11	General Electric	U.S.	168,307.0
12	Ford Motor	U.S.	160,126.0
13	ING Group	Netherlands	158,274.3
14	Citigroup	U.S.	146,777.0
15	AXA	France	139,738.1
16	Volkswagen	Germany	132,323.1
17	Sinopec	China	131,636.0
18	Credit Agricole	France	128,481.3
19	Allianz	Germany	125,346.0
20	Fortis	Belgium/Netherlands	121,201.8
21	Bank of America Corp	U.S.	117,017.0
22	HSBC Holdings	Britain	115,361.0
23	American International Group	U.S.	113,194.0
24	China National Petroleum	China	110,520.2
25	BNP Paribas	France	109,213.6

SOURCE: "World's Largest Corporations," *Fortune*, July 23, 2007, 133.

A multinational company may have several worldwide headquarters, depending on where certain markets or technologies are. Britain's APV, a maker of food-processing equipment, has a different headquarters for each of its worldwide businesses. ABB, Asea Brown Boveri, the European electrical engineering giant based in Zurich, Switzerland, groups its thousands of products and services into 50 or so business areas. Each is run by a leadership team that crafts global business strategy, sets product development priorities, and decides where to make its products. None of the teams work out of the Zurich headquarters; instead, they are scattered around the world. Leadership for power transformers is based in Germany, electric drives in Finland, and process automation in the United States.

The role of multinational corporations in developing nations is a subject of controversy. Multinationals' ability to tap financial, physical, and human resources from all over the world and combine them economically and profitably can benefit any country. They also often possess and can transfer the most up-to-date technology. Critics, however, claim that often the wrong kind of technology is transferred to developing nations. Usually, it is capital-intensive (requiring a greater expenditure for equipment than for labor) and thus does not substantially increase employment. A "modern sector" then emerges in the nation, employing a small proportion of the labor force at relatively high productivity and income levels and with increasingly capital-intensive technologies. In addition, multinationals sometimes support reactionary and oppressive regimes if it is in their best interests to do so. Other critics say that the firms take more wealth out of developing nations than they bring in, thus widening the gap between rich and poor nations. The petroleum industry in particular has been heavily criticized for its actions in some developing countries.

capital-intensive
Using more capital than labor in the production process.

To counter such criticism, more and more multinationals are taking a proactive role in being good global citizens. Sometimes companies are spurred to action by government regulation, and in other cases multinationals are attempting to protect their good brand names.

BLOCKING FOREIGN INVESTMENT

A new backlash against multinational corporations is that governments from China to Canada are placing restrictions on foreign purchases of factories, land, and companies in their countries. This has a major impact on U.S. multinationals because they serve foreign markets primarily through sales in their foreign affiliates and not through exports from the United States. The foreign affiliates manufacture and sell goods locally and rely on local labor and distribution to reach nearby customers.

These new barriers to ownership are partially due to a reaction against globalization. Perhaps more important is the view that the United States is erecting barriers to foreign investment. In 2006, a Dubai-owned company tried to buy operations at five American ports, and, in 2005, the state-owned Chinese oil company Cnooc Ltd. tried to buy California-based oil giant Unocal Corp. Both deals were ultimately voided amid uproar. This prompted Congress to pass legislation to subject foreign investment in the U.S., or to review by the Committee on Foreign Investment in the United States (CFIUS) that screens foreign purchases of U.S. assets with national-security implications.[14]

Now China's new regulations let government officials block a local purchase by a multinational if it is a danger to "economic security." Russia has considered blocking foreign ownership in 39 "strategic sectors" of its economy. If more countries begin to block foreign investment by multinationals, it will definitely have a noticeable impact on global trade.

GLOBAL MARKETING STANDARDIZATION

Traditionally, marketing-oriented multinational corporations have operated somewhat differently in each country. They use a strategy of providing different product features, packaging, advertising, and so on. However, Ted Levitt, a former Harvard professor, described a trend toward what he referred to as "global marketing," with a slightly different meaning.[15] He contended that communication and technology have made the world smaller so that almost all consumers everywhere want all the things they have heard about, seen, or experienced. Thus, he saw the emergence of global markets for standardized consumer products on a huge scale, as opposed to segmented foreign markets with different products. In this book, global marketing is defined as individuals and organizations using a global vision to effectively market goods and services across national boundaries. To make the distinction, we can refer to Levitt's notion as **global marketing standardization**.

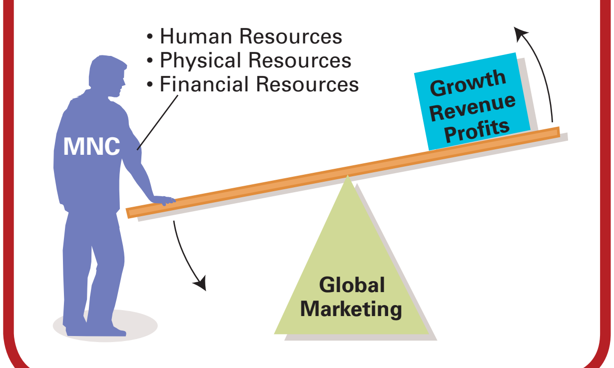
global marketing standardization Production of uniform products that can be sold the same way all over the world.

Global marketing standardization presumes that the markets throughout the world are becoming more alike. Firms practicing global marketing standardization produce "globally standardized products" to be sold the same way all over the world. Uniform production should enable companies to lower production and marketing costs and increase profits. Levitt cited Coca-Cola, Colgate-Palmolive, and McDonald's as successful global marketers. His critics point out, however, that the success of these three companies is really based on variation, not on offering the same product everywhere. McDonald's, for example, changes its salad dressings and provides self-serve espresso for French tastes. It sells bulgogi burgers in South Korea and falafel burgers in Egypt. It also offers different products to suit tastes in Germany (where it offers beer) and Japan (where it offers sake). Further, the fact that Coca-Cola and Colgate-Palmolive sell some of their products in more than 160 countries does not signify that they have adopted a high degree of standardization for all their products globally. Only three Coca-Cola brands are standardized, and one of them, Sprite, has a different formulation in Japan. Some Colgate-Palmolive products are marketed in just a few countries. Axion paste dishwashing detergent, for example, was formulated for developing countries, and La Croix Plus detergent was custom made for the French market. Colgate toothpaste is marketed the same way globally, but its advanced Gum Protection Formula is used in only 27 nations.

Nevertheless, some multinational corporations are moving toward a degree of global marketing standardization. 3M markets some of its industrial tapes the same way around the globe. Procter & Gamble calls its new philosophy "global planning." The idea is to determine which product modifications are necessary from country to country while trying to minimize those modifications. P&G has at least four products that are marketed similarly in most parts of the world: Camay soap, Crest toothpaste, Head and Shoulders shampoo, and Pampers diapers. However, the smell of Camay, the flavor of Crest, and the formula of Head and Shoulders, as well as the advertising, vary from country to country.

REVIEW LEARNING OUTCOME

LO 2 Discuss the impact of multinational firms on the world economy



LO 3
External Environment Facing Global Marketers

A global marketer or a firm considering global marketing must consider the external environment. Many of the same environmental factors that operate in the domestic market also exist internationally. These factors include culture, economic and technological development, political structure and actions, demographic makeup, and natural resources.

CULTURE

Central to any society is the common set of values shared by its citizens that determines what is socially acceptable. Culture underlies the family, the educational system, religion, and the social class system. The network of social organizations generates overlapping roles and status positions. These values and roles have a tremendous effect on people's preferences and thus on marketers' options. A company that does not understand a country's culture is doomed to failure in that country. Cultural blunders lead to misunderstandings and often perceptions of rudeness or even incompetence. For example, when people in India shake hands, they sometimes do so rather limply. This isn't a sign of weakness or disinterest; instead, a soft handshake conveys respect. Avoiding eye contact is also a sign of deference in India.

A U.S. luggage manufacturer found out that culture also affects thinking and perception. The company designed a new Middle East advertising campaign around the image of its luggage being carried on a magic flying carpet. Many of the participants in a group in a marketing research study thought they were seeing advertising for Samsonite *carpets*. Green Giant learned that it could not use its Jolly Green Giant in parts of Asia where wearing a green hat signifies that a man has an unfaithful wife.

Procter and Gamble's research showed that Italians devote 21 hours a week to household chores other than cooking—Americans spend just four hours. They wash kitchen and bathroom floors at least four times a week, compared to the U.S. consumer's once-a-week cleansing. Despite those hours and hours of labor, Italians aren't necessarily a perfect market for convenience products. They want products that are tough cleaners, not timesavers. For example, dishwasher makers targeting the Italian market have had to fight the perception that machines don't get dishes as clean as hand-washing. When Unilever's Cif brand cleaning spray flopped, company research found that Italian women needed convincing that a spray could be strong enough, especially on kitchen grease. The company spent 18 months reformulating the product, testing its power against grease. It changed the focus of advertising from convenience to cleaning ability. And when it was learned that the women felt they needed different cleaners for different tasks, new varieties were created. Containers were also made 50 percent larger because Italians clean so frequently.

P&G's Swiffer Wet mop bombed as a cleaner but research found that Italian women were using it to polish after mopping, so the firm created a Swiffer with beeswax, which it sells only in Italy. Another variety, the Swiffer duster, is sold in many countries but is especially popular in Italy, where it sold five million boxes in its first eight months—twice the company's forecasts. "It was a real shift of mindset on how to market products like these," said Alessandra Bellini, head of marketing for Unilever's home and personal-care products. "If you present a product as quick and easy, women may feel like a cheat . . . It took us a while to understand that Italians didn't want that."[16]

Language is another important aspect of culture. Marketers must take care in translating product names, slogans, instructions, and promotional messages so as not to convey the wrong meaning. For example, Mitsubishi Motors had to rename its Pajero model in Spanish-speaking countries because the term describes a sexual activity. Toyota Motors' MR2 model dropped the number 2 in France because the combination sounds like a French swearword. Coca-Cola had difficulty finding a suitable translation for its name into Mandarin. The transliteration of the syllables of Coca-Cola in Chinese characters could have resulted in Chinese people thinking it read "bite the wax tadpole" or other nonsensical phrases.

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Each country has its own customs and traditions that determine business practices and influence negotiations with foreign customers. In many countries, personal relationships are more important than financial considerations. For instance, skipping social engagements in Mexico may lead to lost sales. Negotiations in Japan often include long evenings of dining, drinking, and entertaining, and only after a close personal relationship has been formed do business negotiations begin. The Japanese go through a very elaborate ritual when exchanging business cards. An American businesswoman was unaware of this important cultural tradition. She came into a meeting and tossed some of her business cards across the table at a group of stunned

Japanese executives. One of them turned his back on her and walked out. The deal never went through.

Making successful sales presentations abroad requires a thorough understanding of the country's culture. Germans, for example, don't like risk and need strong reassurance. A successful presentation to a German client will emphasize three points: the bottom-line benefits of the product or service, that there will be strong service support, and that the product is guaranteed. In southern Europe, it is an insult to show a price list. Without negotiating, you will not close the sale. The English want plenty of documentation for product claims and are less likely to simply accept the word of the sales representative. Scandinavian and Dutch companies are more likely to approach business transactions as Americans do than are companies in any other country.

Never try to do business in Europe in August. Why not? You'll find that everyone has gone on vacation. Today, all European countries have laws requiring companies to provide employees with vacations of at least four weeks (the standard in Belgium, Britain, Germany, and Italy, among others) to five weeks (as in Austria, Denmark, France, and Sweden). But most workers get more vacation time because of collective agreements negotiated by unions or other compensation arrangements.

ECONOMIC AND TECHNOLOGICAL DEVELOPMENT

A second major factor in the external environment facing the global marketer is the level of economic development in the countries where it operates. In general, complex and sophisticated industries are found in developed countries, and more basic industries are found in less developed nations. Average family incomes are higher in more developed countries than those in less developed countries. Larger incomes mean greater purchasing power and demand not only for consumer goods and services but also for the machinery and workers required to produce consumer goods.

According to the World Bank, the combined gross national income (GNI) of the 234 nations for which data are available is approximately $34 trillion. Divide that up among the world's 6.5 billion inhabitants, and you get just $5,230 for every man, woman, and child on Earth. The United States accounts for almost a third of the income earned worldwide, or $12.3 trillion—more than any other single country. If America's GNI were divided equally among its 297 million residents, each American would receive $41,400—6.6 times the world average. Even so, Americans are still not the richest people on the planet. That title goes to the residents of Luxembourg, where the per capita GNI is $56,230.[17]

The most expensive place in the world to live is Moscow (34 percent more expensive than New York, America's most expensive city). Other more expensive places, relative to New York, are: London (26 percent); Seoul (22 percent); Tokyo (22 percent); and Hong Kong (19 percent).[18] A daily newspaper in Moscow costs $6.30. At the other end of the spectrum is Asuncion in Paraguay, which is the least expensive city. It costs about half as much as it does to live in New York.

Doing Business in China and India[19]

The two countries of growing interest to many multinationals are India and China because of their huge economic potential. They have some of the highest growth rates in the world and are emerging as megamarkets. Take cell phones. The number of users in China exceeds 450 million, and the estimated figure for India is 150 million—a number that is growing by six million new subscribers a month.

China and India present different but complementary strengths that multinationals can use. China is much stronger than India in mass manufacturing and logistics; in contrast, India is much stronger than China in software and information-technology services.

Outside the United States, IBM relies on China as the primary source for its hardware business and has decided to relocate its global procurement headquarters

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Haier Group is one of China's fastest-growing companies and one of the world's top brands. In fact, for the third consecutive year, Haier Group was named one of the world's 100-most-recognizable brands in a global name-brand list.

to Shenzhen. Complementing these moves, IBM has made its Indian operations one of its most important global hubs for the delivery of information technology services to clients world-wide. Nearly one-sixth of IBM's global work force is now based in India.

China and India have the world's two largest populations, two of the world's largest geographical areas, greater linguistic and sociocultural diversity than any other country, and among the highest levels of income disparity in the world—some people are extremely poor whereas others are very rich.

Given this scale and variety, there is no "average Chinese customer" or "average Indian customer." In each country, even the middle of the income pyramid consists of more than 300 million people encompassing significant diversity in incomes, geographic climates, cultural habits, and even language and religious beliefs. Because of this diversity, market success in China and India is rarely possible without finely segmenting the local market in each country and developing a strategy tailored to the needs of the targeted segments.

Haier Group, China's leading appliance maker, has proved to be particularly adept at fine market segmentation. The company's line of washing machines for the Chinese market includes a washing machine for rural peasants that can clean not only clothes but also sweet potatoes and peanuts. Haier also sells a tiny washing machine designed to clean a single change of clothes, which has proved to be a hit with the busy urban customers in Shanghai.

POLITICAL STRUCTURE AND ACTIONS

Political structure is the third important variable facing global marketers. Government policies run the gamut from no private ownership and minimal individual freedom to little central government and maximum personal freedom. As rights of private property increase, government-owned industries and centralized planning tend to decrease. But a political environment is rarely at one extreme or the other. India, for instance, is a republic with elements of socialism, monopoly capitalism, and competitive capitalism in its political ideology.

A recent World Bank study found that the least amount of business regulation fosters the strongest economies.[20] The least regulated and most efficient economies are concentrated among countries with well-established common-law traditions, including Australia, Canada, New Zealand, the United Kingdom, and the United States. On a par with the best performers are Singapore and Hong Kong. Not far behind are Denmark, Norway, and Sweden, all social democracies that recently streamlined their business regulation.

The World Bank also found that the poorest countries, which need new businesses and entrepreneurship the most, were the most difficult countries in which to start a new business. Heavy regulation and red tape prevent both economic and job growth. The more roadblocks there are, the more opportunities for underpaid government officials to get kickbacks. But there are also other problems. The World Bank report noted that trade unions prevented Peru from reducing mandatory severance payments, while notaries in Croatia for years have stalled its efforts to simplify procedures to start businesses. It takes 153 days to start a business in Mozambique, for example, but two days in Canada. Enforcing a contract in Indonesia can cost more than the contract's actual value; doing the same in South Korea costs just 5.4 percent of a contract's value.[21]

Legal Considerations

Closely related to, and often intertwined with, the political environment are legal considerations. In France, nationalistic sentiments led to a law that requires pop music stations to play at least 40 percent of their songs in French (even though French teenagers love American and English rock and roll).

Many legal structures are designed to either encourage or limit trade. Here are some examples:

- *Tariff: a tax levied on the goods entering a country*. The United States maintains tariffs as high as 27 percent on Canadian softwood lumber. U.S. lumber producers and environmentalists have alleged that Canada's provincial governments subsidize the softwood industry by charging below-market rates to cut trees and not enforcing environmental laws. Because a tariff is a tax, it will either reduce the profits of the firms paying the tariff or raise prices to buyers or both. Normally, a tariff raises prices of the imported goods and makes it easier for domestic firms to compete. In one case, U.S. shrimpers not only lobbied for tariffs against foreign pond-raised shrimp (which were enacted), but found a way to get even a better deal from foreign shrimpers. The ethics box below explains how this happened.
- *Quota: a limit on the amount of a specific product that can enter a country*. The United States has strict quotas for imported textiles, sugar, and many dairy products. Several U.S. companies have sought quotas as a means of protection from foreign competition. For example, Harley-Davidson convinced the U.S. government to place quotas on large motorcycles imported to the United States. These quotas gave the company the opportunity to improve its quality and compete with Japanese motorcycles.
- *Boycott: the exclusion of all products from certain countries or companies*. Governments use boycotts to exclude companies from countries with which they have a political dispute. Several Arab nations boycotted Coca-Cola because it maintained distributors in Israel.
- *Exchange control: a law compelling a company earning foreign exchange from its exports to sell it to a control agency, usually a central bank*. A company wishing to buy goods abroad must first obtain foreign currency exchange from the control agency. Generally, exchange controls limit the importation of luxuries. For instance, Avon Products drastically cut back new production lines and products in the Philippines because exchange controls prevented the company from converting pesos to dollars to ship back to the home office. The pesos had to be used in the Philippines. China restricts the amount of foreign currency each Chinese company is allowed to keep from its exports. Therefore, Chinese companies must usually get the government's approval to release funds before they can buy products from foreign companies.
- *Market grouping (also known as a common trade alliance): occurs when several countries agree to work together to form a common trade area that enhances trade opportunities*. The best-known market grouping is the European Union (EU), which will be discussed in more detail later. The EU, which was known as the European Community before 1994, has been evolving for more than four decades, yet, until recently, many trade barriers existed among its member nations.
- *Trade agreement: an agreement to stimulate international trade*. Not all government efforts are meant to stifle imports or investment by foreign corporations. The Uruguay Round of trade negotiations is an example of an effort to encourage trade, as was the grant of most favored nation (MFN) status to China by the United States. The largest Latin American trade agreement is **Mercosur,** which includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, and Uruguay. The elimination of most tariffs among the trading partners has

Mercosur
The largest Latin American trade agreement; includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, and Uruguay.

ETHICS in Marketing

U.S. Shrimpers Haul in Cash from Lower Cost Rivals

ETHICS

For the better part of three decades, John Williams made a good living netting shrimp from the Gulf of Mexico. These days, he is landing a different catch: cash payments from foreign rivals. Mr. Williams, executive director of the Southern Shrimp Alliance, co-founded the group in 2002 to help American shrimp fishermen fight competition posed by cheap, pond-raised shrimp from Asia and Latin America. The alliance petitioned the U.S. government to slap tariffs on shrimp imports from six countries at the end of 2003, arguing they were dumping crustaceans in the U.S. at unfairly low prices. But after winning the case—which both raised tariffs and eventually netted $100 million in compensation for U.S. shrimpers—Mr. Williams and his alliance wanted even more. With the help of their New York law firm, the shrimpers filed a special appeal with the U.S. government that threatened the overseas shrimp producers with even higher tariffs. The action spooked more than 100 foreign shrimp suppliers into paying millions of dollars to the U.S. shrimp alliance in return for its promise to drop the action.

The alliance says it is using the money to help the U.S. industry recover from a flood of cheap imports. The payouts have funded lawyers to spearhead trade actions and pay lobbyists to rally government support for the industry, among other priorities. "We now have a voice we never had before," Mr. Williams says.

The practice has sparked a fight over the shrimp alliance's winnings, as well as concern that U.S. shrimpers unjustly exploited laws designed to protect domestic businesses from unfair trading practices. "We know it's unfair, but have to play the game," said Vuong Quang Khanh, head of international sales for Can Tho Import Export Seafood Joint Stock Co., a Vietnamese shrimp exporter that says it paid $68,000 to the shrimp alliance. Dan Ikenson of the Cato Institute, a free-market think tank, says, "There's something unseemly about the domestic industry extorting large sums of money from foreign shrimp producers."[22]

Today foreign producers provide almost 90 percent of the shrimp eaten by Americans each year. Do you think the actions of the Southern Shrimp Alliance are a simple survival effort? Aren't the extra millions paid by foreign shrimpers to the Southern Shrimp Alliance just another tax on U.S. consumers?

resulted in trade revenues of over $16 billion annually. The economic boom created by Mercosur will undoubtedly encourage other nations to seek trade agreements on their own or to enter Mercosur. The European Union hopes to have a free trade pact with Mercosur in the future.

Uruguay Round and Doha Round

Uruguay Round
An agreement to dramatically lower trade barriers worldwide; created the World Trade Organization.

The Uruguay Round is an agreement that has dramatically lowered trade barriers worldwide. Adopted in 1994, the agreement has been signed by 151 nations. It is the most ambitious global trade agreement ever negotiated. The agreement has reduced tariffs by one-third worldwide—a move that is expected to raise global income by $235 billion annually. Perhaps most notable is the recognition of new global realities. For the first time, an agreement covers services, intellectual property rights, and trade-related investment measures such as exchange controls.

The Uruguay Round made several major changes in world trading practices:

- *Entertainment, pharmaceuticals, integrated circuits, and software*: The rules protect patents, copyrights, and trademarks for 20 years. Computer programs receive 50 years of protection and semiconductor chips receive 10 years. But many developing nations were given a decade to phase in patent protection for drugs. France, which limits the number of U.S. movies and TV shows that can be shown, refused to liberalize market access for the U.S. entertainment industry.
- *Financial, legal, and accounting services*: Services came under international trading rules for the first time, creating a vast opportunity for these competitive U.S. industries. Now it is easier for managers and key personnel to be admitted to a country. Licensing standards for professionals, such as doctors, cannot discriminate against foreign applicants. That is, foreign applicants cannot be held to higher standards than domestic practitioners.

World Trade Organization (WTO)
A trade organization that replaced the old General Agreement on Tariffs and Trade (GATT).

General Agreement on Tariffs and Trade (GATT)
A trade agreement that contained loopholes that enabled countries to avoid trade-barrier reduction agreements.

North American Free Trade Agreement (NAFTA)
An agreement between Canada, the United States, and Mexico to reduce trade barriers between the countries.

- *Agriculture*: Europe is gradually reducing farm subsidies, opening new opportunities for such U.S. farm exports as wheat and corn. Japan and Korea are beginning to import rice. But U.S. growers of sugar and citrus fruit have had their subsidies trimmed.
- *Textiles and apparel*: Strict quotas limiting imports from developing countries are being phased out, causing further job losses in the U.S. clothing trade. But retailers and consumers are the big winners, because past quotas have added $15 billion a year to clothing prices.
- *A new trade organization*: The World Trade Organization (WTO) replaced the old General Agreement on Tariffs and Trade (GATT), which was created in 1948. The old GATT contained extensive loopholes that enabled countries to avoid the trade-barrier reduction agreements—a situation similar to obeying the law only if you want to! Today, all WTO members must fully comply with all agreements under the Uruguay Round. The WTO also has an effective dispute settlement procedure with strict time limits to resolve disputes.

The latest round of WTO trade talks began in Doha, Qatar, in 2001. For the most part, the periodic meetings of WTO members under the Doha Round have been very contentious. Typically, the discussions find developing countries on one side of the argument and rich developed countries on the other. A major goal of the Doha Round is to bolster the developing economies of Africa, Asia, and Latin America, where up to two-thirds of the population work in agriculture. To this end, efforts have been made to persuade the developed countries to lower their barriers on food imports and reduce the subsidies they provide to their own farmers. It has been estimated that if rich countries agreed to eliminate their barriers to imports from poor countries, approximately 270 million people would be lifted out of poverty.[23] At the same time, the United States hopes to end the rampant piracy of patents and copyrights in developing countries, to increase opportunities abroad for U.S. service companies, and to obtain lower tariffs for U.S. exports to other countries.

Negotiations collapsed when the developing nations, led by Brazil, India, and China, demanded that the United States and the European Union drop agricultural tariffs and slash domestic agricultural subsidies faster and deeper than either was willing to do. The $300 billion a year in domestic subsidies to farmers encourages huge amounts of excess production. This, in turn, depresses global agricultural prices and makes it difficult, or impossible, for developing countries to compete. France, in particular, has balked at trimming subsidies to its inefficient farmers and has threatened to capsize a modest EU subsidy-trimming plan. For their part, developing nations, led by Brazil and India, have threatened to retain import barriers and continue making knockoff pharmaceuticals and software.

When this text went to press, the Doha talks continued to be at a stalemate. Doha largely ignored trade in services, even though many economists believe that the consumer benefits from liberalization of services—from advertising to banking—are far greater than the remaining opportunities in goods trade. If Doha ultimately fails, it may set the stage for the erosion of the WTO's role as the principal forum for addressing not just trade, but the broader process of globalization.

The trend toward globalization has resulted in the creation of additional agreements and organizations: the North American Free Trade Agreement, the Central America Free Trade Agreement, the European Union, the World Bank, and the International Monetary Fund.

North American Free Trade Agreement

At the time it was instituted, the North American Free Trade Agreement (NAFTA) created the world's largest free trade zone at that time. Ratified by the U.S. Congress in 1993, the agreement includes Canada, the United States, and Mexico, with a combined population of 360 million.

Canada, the largest U.S. trading partner, entered a free trade agreement with the United States in 1988. Thus, many of the new long-run opportunities for U.S. business under NAFTA have been in Mexico, America's second largest trading partner. Tariffs on Mexican exports to the United States averaged just 4 percent before the treaty was signed, and most goods entered the United States duty-free. Therefore, the main impact of NAFTA was to open the Mexican market to U.S. companies. When the treaty went into effect, tariffs on about half the items traded across the Rio Grande disappeared. The pact removed a web of Mexican licensing requirements, quotas, and tariffs that limited transactions in U.S. goods and services. For instance, the pact allowed U.S. and Canadian financial-services companies to own subsidiaries in Mexico for the first time in 50 years.

In August 2007, the three member countries met in Canada to "tweak" NAFTA, but made no substantial changes. For example, the members agreed to further remove trade barriers on hogs, steel, consumer electronics, and chemicals. They also directed the North American Steel Trade Committee, which represents the three governments, to focus on subsidized steel from China. Most Canadians (73 percent) and Americans (77 percent) feel that NAFTA has played a key role in North American prosperity.[24] The survey was not conducted in Mexico.

The real question is whether NAFTA can continue to deliver rising prosperity in all three countries. America has certainly benefited from cheaper imports and more investment opportunities abroad. Over the years, Mexico has also made huge economic gains due to NAFTA. The U.S.-Mexico cross border trade now averages over $750 million a day.[25] Over $1 billion in trade flows daily between the United States and Canada. During the 1990s, many Canadian manufacturers switched from producing a broad cross section of products to higher-value niche-products that were less prone to competitive pressures such as wood products, clothing, and transportation equipment.

Although Mexico has thrived under NAFTA, its prospects are not as bright as in the past. It is losing its advantage as a low-cost producer to countries such as India and China. American businesses complain that Mexico has a dysfunctional judicial system, unreliable power supplies, poor roads, high corporate tax rates, and unfriendly labor relations. This has given companies pause when considering investing in Mexico. Mexico still has a lot to offer, but it must improve its infrastructure.

Central America Free Trade Agreement

Central America Free Trade Agreement (CAFTA)
A trade agreement, instituted in 2005, that includes Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and the United States.

The newest free trade agreement is the Central America Free Trade Agreement (CAFTA) instituted in 2005. Besides the United States, the agreement includes Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua. The United States is already the principal exporter to these nations, so economists think that it will not result in a major increase in U.S. exports. It will, however, reduce tariffs on exports to CAFTA countries. Already, some 80 percent of the goods imported into the United States from CAFTA nations are tariff-free. CAFTA countries may benefit from the new permanent trade deal if U.S. multinational firms deepen their investment in the region. In the first two years after CAFTA was founded, trade increased in all CAFTA countries, including the U.S.[26]

How Does the U.S. Engage in Global Trade?

Now that you understand the various entities in global trade, let's examine how America trades. The U.S. participates in three kinds of trade agreements:

- The U.S. has bilateral agreements (agreements between two nations). In 2007, the United States and Korea signed a bilateral trade agreement. It is estimated to expand trade between the two countries by $20 billion per year. Over a three-year period, 95 percent of the tariffs and other trade barriers between the two nations will be eliminated.[27]

- The U.S. is a member of several regional agreements, including NAFTA and CAFTA.
- The U.S. participates in multilateral agreements (agreements among many nations), including the World Trade Organization.

European Union

European Union
A free trade zone encompassing 27 European countries.

One of the world's most important free trade zones is the European Union (EU), which now encompasses most of Europe. More than a free trade zone, it is also a political and economic community. As a free trade zone it guarantees the freedom of movement of people, goods, services, and capital between member states. It also maintains a common trade policy with outside nations and a regional development policy. The EU represents member nations in the WTO. Recently, the EU also began venturing into foreign policy as well, dealing with Iran's uranium refinement.

The European Union currently has 27 member states: Austria, Belgium, Bulgaria, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, and the United Kingdom (see Exhibit 5.3). There are currently three official candidate countries, Croatia, the Republic of Macedonia, and Turkey. In addition, the western Balkan countries of Albania, Bosnia and Herzegovina, Montenegro, and Serbia are officially recognized as potential candidates.[28]

To join the EU, a country must meet the Copenhagen criteria, defined at the 1993 Copenhagen European Council. These require a stable democracy which

Exhibit 5.3
The European Union

SOURCE: © European Community

respects human rights and the rule of law; a functioning market economy capable of competition within the EU; and the acceptance of the obligations of membership, including EU law. Evaluation of a country's fulfillment of the criteria rests with the European Council.[29]

Governance The government of the EU consists of a number of institutions, primarily the Commission, Council, and Parliament. The European Commission is the EU's executive branch and is responsible for the day-to-day running of the EU. It is currently composed of 27 commissioners, one from each member state. The Council of the European Union (also known as the Council of Ministers) forms part of the EU's legislative branch, the other being the Parliament. The Council consists of the national ministers responsible for the specific area of the EU law being addressed. For example, European legislation regarding agriculture would be treated by a Council composed of the national ministers for agriculture. The body's presidency rotates between the member states every six months.

The other half of the legislative branch is the European Parliament, which is the only directly elected institution. The 785 Members of the European Parliament are directly elected by European citizens every five years (the last full election was in 2004; the next election is scheduled for June 2009). Although the elections are in national constituencies, the members are seated in the meeting room according to political groups rather than nationality. The institution has near-equal legislative powers with the Council in community matters and has the power to reject or censure the Commission.[30]

The European Union Commission and the courts have not always been kind to U.S. multinationals. First, the EU court blocked a merger between two U.S. companies—General Electric and Honeywell. In late 2007, it concluded that Microsoft used its dominance in desktop computer software to muscle into server software and media players. The EU courts said that Microsoft blocked competition and fined the company $613 million.[31] Before acquiring Double Click (a company that tracks web surfing), Google asked the European Commission to first approve the proposed merger.

The Importance of the EU to the United States The European Union is the largest economy in the world. It has a gross domestic product of about $18 trillion, compared with about $11.5 trillion for the United States. Unemployment is at its lowest level in at least 15 years. In 2006, labor productivity matched that of the U.S. again, for the first time in many years.[32]

The EU is also a huge market, with a population of nearly 500 million. The U.S. and EU have the largest bilateral trade and investment relationship in world history. Together, they account for more than half of the global economy, while bilateral trade accounts for 7 percent of the world total. U.S. and EU companies have invested an estimated $2 trillion in each other's economies, employing directly and indirectly as many as 14 million workers. Nearly every U.S. state is involved with exporting to, importing from, or working for European firms. Even California, with its close economic ties to Asia, has roughly 1 million workers connected to European investment or trade.[33]

Some economists have called the EU the "United States of Europe." It is an attractive market, with a huge amount of purchasing power. But the EU will probably never be a United States of Europe. For one thing, even if a united Europe achieves standardized regulations, marketers will not be able to produce a single Europroduct for a generic Euroconsumer. With more than 15 different languages and individual national customs, Europe will always be far more diverse than the United States. Thus, product differences will continue to be necessary. It will be a long time, for instance, before the French begin drinking the instant coffee that the British enjoy. Preferences for washing machines also vary: British homemakers want front-loaders, and the French want top-loaders; Germans like lots of settings and high spin speeds; Italians like lower speeds. Even European companies that think they understand Euroconsumers often have difficulties producing "the right product." Atag Holdings NV, a diversified Dutch company whose main business is kitchen appliances, was confident it could cater to both the "potato" and "spaghetti" belts—marketers' terms for consumer preferences in northern and southern Europe. But Atag quickly discovered that preferences extend beyond food preferences. For example, on its ovens, burner shape and size, knob and clock placement, temperature range, and colors vary greatly from country to country. Although Atag's kitchenware unit has lifted foreign sales to 25 percent of its total from 4 percent in the mid-1990s, it now believes that its range of designs, and its speed in delivering them, rather than the magic bullet of a Europroduct, will keep it competitive.

An entirely different type of problem facing global marketers is the possibility of a protectionist movement by the EU against outsiders. For example, European automakers have proposed holding Japanese imports at roughly their current 10 percent market share. The Irish, Danes, and Dutch don't make cars and have unrestricted home markets; they would be unhappy about limited imports of Toyotas and Nissans. But France has a strict quota on Japanese cars to protect Renault and Peugeot. These local carmakers could be hurt if the quota is raised at all.

The World Bank and International Monetary Fund

Two international financial organizations are instrumental in fostering global trade. The World Bank offers low-interest loans to developing nations. Originally, the purpose of the loans was to help these nations build infrastructure such as roads, power plants, schools, drainage projects, and hospitals. Now, the World Bank offers loans to help developing nations relieve their debt burdens. To receive the loans, countries must pledge to lower trade barriers and aid private enterprise. In addition to making loans, the World Bank is a major source of advice and information for developing nations. The United States has granted the organization $60 million to create knowledge databases on nutrition, birth control, software engineering, creating quality products, and basic accounting systems.

World Bank
An international bank that offers low-interest loans, advice, and information to developing nations.

International Monetary Fund (IMF)
An international organization that acts as a lender of last resort, providing loans to troubled nations, and also works to promote trade through financial cooperation.

Recently, the World Bank said that it would sharply increase aid to the poorest nations. Between 2007 and 2009, the World Bank plans to funnel $3.5 billion to the International Development Association.[34] That program provides money for development projects in the world's most impoverished countries, mostly in Africa. The World Bank also cancelled the debts of 19 of its poorest borrowers.

The International Monetary Fund (IMF) was founded in 1945, one year after the creation of the World Bank, to promote trade through financial cooperation and eliminate trade barriers in the process. The IMF makes short-term loans to member nations that are unable to meet their budgetary expenses, operating as a lender of last resort for troubled nations. In exchange for these emergency loans, IMF lenders frequently extract significant commitments from the borrowing nations to address the problems that led to the crises. These steps may include curtailing imports or even devaluing the currency.

DEMOGRAPHIC MAKEUP

The three most densely populated nations in the world are China, India, and Indonesia. But that fact alone is not particularly useful to marketers. They also need to know whether populations are mostly urban or rural, because marketers may not have easy access to rural consumers. In Belgium, about 90 percent of the population lives in an urban setting, whereas in Kenya, almost 80 percent of the population lives in a rural setting. Belgium is thus the more attractive market. Just as significant as population is personal income within a country.

Another key demographic consideration is age. There is a wide gap between the older populations of the industrialized countries and the vast working-age populations of developing countries. This gap has enormous implications for economies, businesses, and the competitiveness of individual countries. It means that while Europe and Japan struggle with pension schemes and the rising cost of health care, countries like China, Brazil, and Mexico can reap the fruits of what's known as a demographic dividend: falling labor costs, a healthier and more educated population, and the entry of millions of women into the workforce.

The demographic dividend is a gift of falling birthrates, and it causes a temporary bulge in the number of working-age people. Population experts have estimated that one-third of East Asia's economic miracle can be attributed to a beneficial age structure. But the miracle occurred only because the governments had policies in place to educate their people, create jobs, and improve health.

NATURAL RESOURCES

A final factor in the external environment that has become increasingly evident in the past decade is the shortage of natural resources. For example, petroleum shortages have created huge amounts of wealth for oil-producing countries such as Norway, Saudi Arabia, and the United Arab Emirates. Both consumer and industrial markets have blossomed in these countries. Other countries—including Indonesia, Mexico, and Venezuela—were able to borrow heavily against oil reserves in order to develop more rapidly. On the other hand, industrial countries like Japan, the United States, and much of western Europe have lost wealth to the petroleum-rich nations. The high price of oil has created inflationary pressures in petroleum-importing nations. It also created major problems for airlines and other petroleum-dependent industries.

Petroleum is not the only natural resource that affects international marketing. Warm climate and water scarcity mean that many of Africa's countries will continue importing foodstuffs. The United States, on the other hand, must rely on Africa for many precious metals. Japan depends heavily on the United States for timber and logs. A Minnesota company manufactures and sells a million pairs of disposable chopsticks to Japan each year. The list could go on, but the point is clear. Vast differences in natural resources create international dependencies, drive huge shifts of wealth, influence inflation and recession, generate export opportunities for countries with abundant resources, and may even stimulate military intervention.

REVIEW LEARNING OUTCOME

LO3 **Describe the external environment facing global marketers**

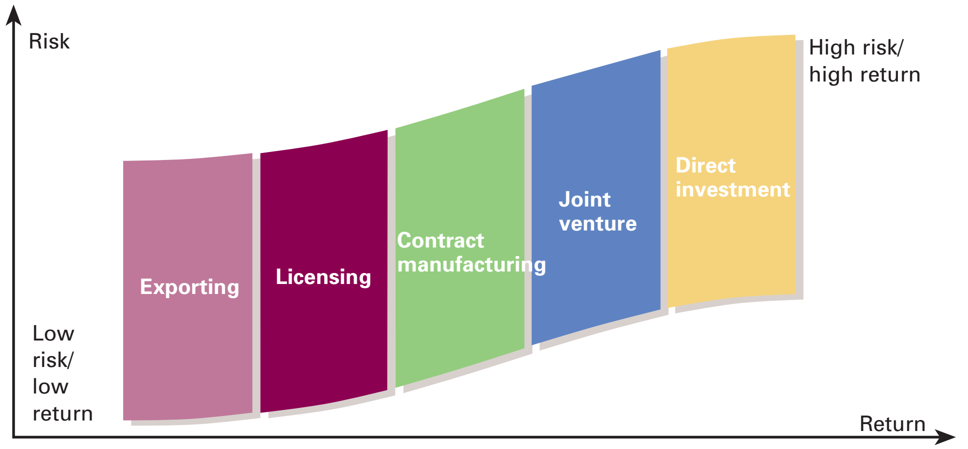
LO4 Global Marketing by the Individual Firm

A company should consider entering the global marketplace only after its management has a solid grasp of the global environment. Some relevant questions are "What are our options in selling abroad?" "How difficult is global marketing?" and "What are the potential risks and returns?" Concrete answers to these questions would probably encourage many strictly domestic U.S. firms to venture into the international arena. Foreign sales can be an important source of profits.

Companies decide to "go global" for a number of reasons. Perhaps the most important is to earn additional profits. Managers may feel that international sales will result in higher profit margins or more added-on profits. A second stimulus is that a firm may have a unique product or technological advantage not available to other international competitors. Such advantages should result in major business

Exhibit 5.4

Risk Levels for Five Methods of Entering the Global Marketplace



successes abroad. In other situations, management may have exclusive market information about foreign customers, marketplaces, or market situations. While exclusivity can provide an initial motivation for international marketing, managers should that competitors to catch up with the firm's information advantage. Finally, saturated domestic markets, excess capacity, and potential for economies of scale can also be motives "going global." Economies of scale mean that average per-unit production costs fall as output is increased.

Many firms form multinational partnerships—called strategic alliances—to assist them in penetrating global markets; strategic alliances are examined in Chapter 7. Five other methods of entering the global marketplace are, in order of risk, exporting, licensing and franchising, contract manufacturing, joint ventures, and direct investment (see Exhibit 5.4).

EXPORTING

exporting
Selling domestically produced products to buyers in another country.

When a company decides to enter the global market, exporting is usually the simplest and least risky option. Exporting is selling domestically produced products to buyers in another country. A company can sell directly to foreign importers or buyers. Exporting is not limited to huge corporations like General and 3M. Indeed, small companies account for 96 percent of all U.S. exporters, but only 30 percent of the export volume.[35] The United States is the world's largest exporter.

The U.S. Commercial Service within the Department of Commerce promotes itself as "Your Global Business Partner." It offers trade specialists in more than 100 U.S. cities and 150 overseas offices to assist beginning exporters, and helps those already engaged in global marketing increase their business. The primary services offered by the U.S. Commercial Service are marketing research, locating qualified buyers and partners, trade events, and global business consulting. These services are explained in more detail in Exhibit 5.5.

The federal government has created a new Web site, **www.export.gov**, that brings together all of the resources across the U.S. government to assist American firms that wish to go global. The site directs you to the U.S. Commercial Service for things like marketing research and trade leads, the Export-Import Bank for loan information, and the U.S. Department of Agriculture for agricultural export assistance. In all, **www.export.gov** brings together nineteen federal agencies that offer some form of export assistance. The Export-Import Bank helps U.S. firms export goods and services. It doesn't compete directly with private banks, but provides export financing to fill gaps in trade financings. That is, the Export-Import Bank assumes credit and country risks that the private sector is unable or unwilling to accept. About 85 percent of the Export-Import Bank's financing is to small businesses.[36] For those interested in international business, a nongovernmental Web site offering links to hundreds of useful sites is available from the International Federation of International Trade Associations (**http://fita.org**).

Exhibit 5.5

Assistance Provided by the U.S. Commercial Service to Exporters

COUNSELING AND ADVOCACY

- **Advocacy:** Get a competitive edge with U.S. Commercial Service advocacy. U.S. diplomats and other officials help your company when unanticipated problems arise—resolve payment issues, settle disputes, win contracts, and overcome regulatory hurdles. Support can include government-to-government meetings by U.S. Commercial Service officers and ambassadors with high-level foreign government officials, in addition to direct intervention with international companies.
- **Counseling:** Increase your export sales and enter new international markets with U.S. Commercial Service export counseling. Trade specialists in more than 100 U.S. cities and 80 countries provide in-depth export consulting and customized business solutions. Our trade specialists near you work with our team of experts overseas in getting you the information and advice that you need to succeed.
- **Platinum Key Service:** Get long-term, comprehensive, customized support to achieve your business goals. The Platinum Key Service is solution oriented and custom-tailored to your needs. Identify markets, launch products, develop major project opportunities, resolve market entry questions, and receive assistance on regulatory matters. Our in-country trade specialists will work closely with you to identify needs, provide progress reports, and ensure timely resolution.

MARKET RESEARCH

- **Market Research Library:** Accurate, up-to-date information lets you target the best international markets. Our comprehensive market research includes overviews on doing business in more than 120 countries and profiles of 110 industry sectors. You can also get updates on new regulations, currency fluctuations, business trends, and government-financed projects. Much of this research is available at no charge.
- **Customized Market Research:** Receive specific intelligence on the export prospects for your product or service in a potential market.
- **Business Facilitation Service:** Get low-cost logistical and administrative support when you're on international business travel. Our Business Facilitation Service offers flexible solutions to let you do business when you're away from home.

FINDING INTERNATIONAL PARTNERS

- **International Partner Search:** Find qualified international buyers, partners, or agents without traveling overseas. U.S. Commercial Service specialists will deliver detailed company information on up to five prescreened international companies that have expressed an interest in your company's products and services.
- **Gold Key Matching Service:** Save time and money by letting the U.S. Commercial Service help you find a buyer, partner, agent, or distributor. The Gold Key Service provides you with one-on-one appointments with prescreened potential agents, distributors, sales representatives, association and government contracts, licensing or joint venture partners, and other strategic business partners in your targeted export market.
- **Commercial News USA:** Promote your products and services to more than 400,000 international buyers in 145 countries. Commercial News USA is a product catalog distributed by U.S. embassies and consulates worldwide and has a proven track record of high response rates and solid sales results.
- **Trade Leads:** View announcements from qualified international companies looking to source U.S. products and services and advertise government tender projects through our trade leads database. All of our trade leads are prescreened by our U.S. embassy or consulate staff overseas and are provided as a free service for U.S. exporters.
- **International Company Profile:** Prevent costly mistakes with quick, low-cost credit checks or due-diligence reports on international companies. Before you do business with a prospective agent, distributor, or partner, the International Company Profile will give you the background information you need to evaluate the company.

TRADE EVENTS AND RELATED SERVICES

- **U.S. Pavilions at Certified Trade Fairs:** Exhibit at U.S. Pavilions certified by the U.S. Commercial Service and increase your chances of finding new business. Certified U.S. Pavilions offer one-on-one business matching, business counseling from trade specialists, and special exhibit services designed to help U.S. exporters maximize returns from trade shows and make more international sales.

- **Trade Fair Certification:** Exhibiting at a trade show abroad can lead to tremendous export opportunities for U.S. companies. This is why the Trade Fair Certification Program was created: to help companies like yours make important exhibiting decisions and free you of many of the concerns you may have about exhibiting outside the United States.
- **International Buyer Program:** Find new international business partners at U.S. trade shows with the International Buyer Program. The IBP recruits more than 125,000 foreign buyers and distributors to 32 top U.S. trade shows per year. U.S. Commercial Service trade specialists arrange meetings for U.S. exporters and international delegates and provide export counseling at the show's International Business Center.
- **Trade Missions:** Meet face-to-face with prescreened international business contacts in promising markets with U.S. Commercial Service trade missions. Trade missions save you time and money by allowing you to maximize contact with qualified distributors, sales representatives, or partners in one to four countries.
- **Virtual Trade Missions:** If your schedule or travel budget limits your ability to travel overseas, consider Virtual Trade Missions. An interactive two-hour videoconference lets you meet virtually. Planning an International Trade Mission? Every year, the U.S. Commercial Service supports dozens of trade missions organized by state economic organizations, elected officials, chambers of commerce, and industry associations through our Certified Trade Mission program.
- **Catalog Events:** Looking for an affordable, low-risk way to promote your products and services in promising markets throughout the world? Increase your company's international sales potential by showcasing your products and services with the International Catalog Exhibition Program.
- **Trade Specialists:** U.S. Commercial Service trade specialists located in international markets will translate your company profile into the local language, display your marketing materials, collect sales leads from interested local buyers, and then assist you as you follow up with the local contacts.

SOURCE: U.S. Commercial Service

buyer for export
An intermediary in the global market that assumes all ownership risks and sells globally for its own account.

export broker
An intermediary who plays the traditional broker's role by bringing buyer and seller together.

export agent
An intermediary who acts like a manufacturer's agent for the exporter. The export agent lives in the foreign market.

licensing
The legal process whereby a licensor agrees to let another firm use its manufacturing process, trademarks, patents, trade secrets, or other proprietary knowledge.

Instead of selling directly to foreign buyers, a company may decide to sell to intermediaries located in its domestic market. The most common intermediary is the export merchant, also known as a buyer for export, which is usually treated like a domestic customer by the domestic manufacturer. The buyer for export assumes all risks and sells internationally for its own account. The domestic firm is involved only to the extent that its products are bought in foreign markets.

A second type of intermediary is the export broker, who plays the traditional broker's role by bringing buyer and seller together. The manufacturer still retains title and assumes all the risks. Export brokers operate primarily in agricultural products and raw materials.

Export agents, a third type of intermediary, are foreign sales agents-distributors who usually live in the foreign country and perform the same functions as domestic manufacturers' agents, helping with international financing, shipping, and so on. The U.S. Department of Commerce has an agent-distributor service that helps about 5,000 U.S. companies per year find an agent or distributor in virtually any country. A second category of agents resides in the manufacturer's country but represents foreign buyers. This type of agent acts as a hired purchasing agent for foreign customers operating in the exporter's home market.

LICENSING AND FRANCHISING

Another effective way for a firm to move into the global arena with relatively little risk is to sell a license to manufacture its product to someone in a foreign country. Licensing is the legal process whereby a licensor allows another firm to use its manufacturing process, trademarks, patents, trade secrets, or other proprietary knowledge. The licensee, in turn, pays the licensor a royalty or fee agreed on by both parties.

Because licensing has many advantages, U.S. companies have eagerly embraced the concept, sometimes in unusual ways. Caterpillar, the producer of heavy machinery, has licensed Wolverine World Wide to make "CAT" brand shoes and boots. Europeans have latched onto CAT gear as the new symbol of American outdoor culture. CAT is one of Europe's hottest brands, which translates into almost $1 billion in licensing revenues.

A licensor must make sure it can exercise sufficient control over the licensee's activities to ensure proper quality, pricing, distribution, and so on. Licensing may also create a new competitor in the long run, if the licensee decides to void the license agreement. International law is often ineffective in stopping such actions. Two common ways to maintain effective control over licensees are shipping one or more critical components from the United States or locally registering patents and trademarks to the U.S. firm, not to the licensee. Garment companies maintain control by delivering only so many labels per day; they also supply their own fabric, collect the scraps, and do careful unit counts.

Entertainment characters and properties, such as Celine Dion, Antonio Banderas, and SpongeBob SquarePants, account for 24 percent of worldwide retail sales of licensed goods. Total license sales now run over $110 billion annually. Corporate trademark/brand properties and fashion labels each account for 21 percent of the total. The United States and Canada account for 65 percent of all global licensing sales.[37]

Franchising is a form of licensing that has grown rapidly in recent years. More than 400 U.S. franchisors operate more than 40,000 outlets in foreign countries, bringing in sales of over $9 billion.[38] Over half of the international franchises are for fast-food restaurants and business services. Relationships with franchisees are not always harmonious, however. Coca-Cola Femsa, Coke's biggest bottler in Latin America and its second largest worldwide, was upset to learn from Coke USA that prices for beverage concentrate—the main ingredient in soft drinks and Coke's primary source of income—would gradually increase in Mexico, starting in 2007. Femsa officials said the price rise cost the company an additional $20 million in 2007 and an extra $60 million annually by 2009. They plan to cut their marketing dollars on Coke's sodas "to offset the impact to our profitability that such concentrate prices represent." Coke's second largest bottler in Mexico, Embotelladoras Arca, said it was considering a similar cutback in marketing.[39]

Franchisors cannot always offer the same product or the same method of distribution in countries around the globe. Domino's Pizza, for example, found that in Japan it had to modify its delivery procedures because addresses there often aren't sequential but instead are determined by a building's age. On Aruba, it soon found that using motorcycles to deliver pizzas was too dangerous because of the island's strong winds. (Small trucks solved the problem.) In the Philippines, locations of stores at times were chosen using feng shui, a Chinese art that positions buildings according to spiritual flows. And because many Icelanders stay up all hours, Domino's stores there must be open much longer than elsewhere. When the company went into Italy, many Italians found its pizza "too American—the sauce being too bold, the toppings too heavy," a company spokesman recalls.[40]

CONTRACT MANUFACTURING

contract manufacturing
Private-label manufacturing by a foreign company.

Firms that do not want to become involved in licensing or to become heavily involved in global marketing may engage in **contract manufacturing**, which is private-label manufacturing by a foreign company. The foreign company produces a certain volume of products to specification, with the domestic firm's brand name on the goods. The domestic company usually handles the marketing. Thus, the domestic firm can broaden its global marketing base without investing in overseas plants and equipment. After establishing a solid base, the domestic firm may switch to a joint venture or direct investment.

Recently, particularly in China, contract manufacturers have been making overruns and selling the excess production directly to either consumers or retailers. New Balance, for example, found that a contract manufacturer was producing extra running shoes and selling them to unauthorized retailers. The retailers were selling the knockoff New Balance shoes for $20, while authorized retailers were trying to sell the same shoe for $60. Recently, New Balance changed its relationship with its suppliers. It cut the number of factories it uses in China to six and now monitors them more closely. It also began using high-tech shoe labels to better spot counterfeits and maintain control of its own production. These steps didn't solve all of New Balance's problems. One contract manufacturer, Horace Chang, produced a shoe called "the classic," a low-tech shoe without the midsole engineering that defines a high performance shoe. Unhappy with Mr. Chang because of "overproduction," New Balance terminated the contract and asked for molds, specifications, signs, labels, packages, wrappers, and ads. Mr. Chang did not return the materials and continued selling in Taiwan, Hong Kong, Italy, and Germany. In addition, he launched a competing brand called "Henkees." A long court battle in China was ineffectual. Finally, an American international arbitrator awarded New Balance $9.9 million.[41] To date, the firm hasn't collected a penny. Yet New Balance still uses contract manufacturing in China because the market is too important to pass up.

Today there are three terms used to describe brand theft:

- *Counterfeit* – a product that bears a trademark that its maker had no authority to use.
- *Knockoff* – a broad term encompassing both counterfeits and items that look like branded products, though they don't actually bear forged trademarks.
- *Third shift* – an unauthorized product made by an unauthorized or authorized contractor. Thus, a contract manufacturer may use two production shifts to produce authorized product and a third shift to produce goods to be sold through an unauthorized channel. The contract manufacturer gets all of the revenue from production.

joint venture
When a domestic firm buys part of a foreign company or joins with a foreign company to create a new entity.

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Many U.S. companies practice direct investment by building manufacturing or marketing facilities in foreign countries, like the Chinese Wal-Mart Supercenter pictured here.

JOINT VENTURE

Joint ventures are somewhat similar to licensing agreements. In an international **joint venture**, the domestic firm buys part of a foreign company or joins with a foreign company to create a new entity. A joint venture is a quick and relatively inexpensive way to go global and to gain needed expertise.[42] For example, Robert Mondavi Wineries entered into a joint venture with Baron Philippe de Rothschild, owner of Bordeaux's First Growth chateau, Mouton-Rothschild. They created a wine in California called Opus One. It was immediately established as the American vanguard of quality and price. Mondavi has entered other joint ventures with the Frescobaldi family in Tuscany and with Errazuriz in Chile.

Joint ventures can be very risky. Many fail; others fall victim to a takeover, in which one partner buys out the other. Sometimes joint venture partners simply can't agree on management strategies and policies. Though joint ventures are very popular in the auto industry, many have not worked out. Joint venture factories—General Motors/Toyota, Suzuki/GM, Mazda/Ford, DaimlerChrysler/Mitsubishi—have not been particular successes. GM has a 50-50 joint venture with the Shanghai

Automotive Corporation, owned by the Shanghai city government. The joint venture, founded in 1997, makes Buicks, Cadillacs, and Chevrolets. It has created hundreds of millions of dollars profit for GM. Now, the Chinese company, using the technology and the money earned from selling joint-venture cars, is becoming a serious competitor to GM; the Chinese Roewe is said to be bigger and more luxurious than the American Buick. The chairman of Shanghai Automotive says, "We now want to build a global Chinese brand."[43]

DIRECT INVESTMENT

direct foreign investment
Active ownership of a foreign company or of overseas manufacturing or marketing facilities.

Active ownership of a foreign company or of overseas manufacturing or marketing facilities is **foreign direct investment.** Direct foreign investment by U.S. firms is currently about $2,100 billion. Direct investors have either a controlling interest or a large minority interest in the firm. Thus, they have the greatest potential reward and the greatest potential risk. Because of the problems discussed above with contract manufacturing and joint ventures in China, multinationals are going it alone. Today, nearly five times as much foreign direct investment comes into China in the form of stand-alone efforts as comes in for joint ventures.[44]

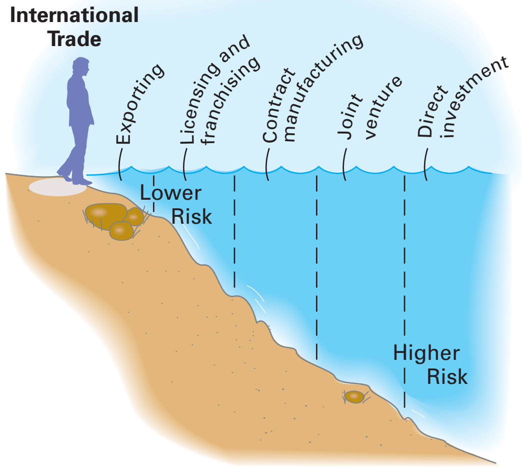
Wal-Mart now has over 2,000 stores located outside the United States. In 2006, international sales accounted for 20 percent of total sales. About one-third of all new Wal-Mart stores are opened in global markets. Wal-Mart already has 151 stores in Brazil, for example, and is opening about two more there each month. Today, the company reaches about half of Brazil's 180 million consumers. Wal-Mart's total sales of $300 billion almost equal half of Brazil's GDP.[45] Wal-Mart occasionally stumbles in its quest for international growth. Wal-Mart found that local discounters undercut its prices in Germany and eventually pulled out of the German market, losing $1 billion. It also left the South Korean market.[46] Also, Wal-Mart has spent more than $1 billion in Japan, but its Seiyu stores are struggling to overcome apathy and employee disinterest.[47] It may just be a matter of time before the firm exits Japan. Yet Wal-Mart is dominating the Latin American market. It is the biggest single retailer in Latin America and the largest private employer in Mexico. Sales at Wal-Mex, its Mexican unit, were $21 billion in 2007.[48]

A firm may make a direct foreign investment by acquiring an interest in an existing company or by building new facilities. It might do so because it has trouble transferring some resource to a foreign operation or getting that resource locally. One important resource is personnel, especially managers. If the local labor market is tight, the firm may buy an entire foreign firm and retain all its employees instead of paying higher salaries than competitors. For example, when Wal-Mart decided to enter China it purchased the general merchandise chain Trust-Mart for about $1 billion.[49]

The United States is a popular place for direct investment by foreign companies. In 2008, the value of foreign-owned businesses in the United States was more than $650 billion. For example, in 2007 Taiwan-based Aur bought U.S. computer maker Gateway. Two years earlier, China's Lenovo Group purchased the PC operations of IBM.

REVIEW LEARNING OUTCOME

LO4 Identify the various ways of entering the global marketplace



LO5

The Global Marketing Mix

To succeed, firms seeking to enter into foreign trade must still adhere to the principles of the marketing mix. Information gathered on foreign markets through research is the basis for the four Ps of global marketing strategy: product, place (distribution), promotion, and price. Marketing managers who understand the advantages and disadvantages of different ways to enter the global market and the effect of the external environment on the firm's marketing mix have a better chance of reaching their goals.

The first step in creating a marketing mix is developing a thorough understanding of the global target market. Often this knowledge can be obtained through the same types of marketing research used in the domestic market (see Chapter 9). However, global marketing research is conducted in vastly different environments. Conducting a survey can be difficult in developing countries, where Internet ownership is growing but still uncommon and mail delivery is slow or sporadic. Drawing samples based on known population parameters is often difficult because of the lack of data. In some cities in South America, Mexico, Africa, and Asia, street maps are unavailable, streets are unidentified, and houses are unnumbered. Moreover, the questions a marketer can ask may differ in other cultures. In some cultures, people tend to be more private than in the United States and will not respond to personal questions on surveys. For instance, in France, questions about one's age and income are considered especially rude.

PRODUCT AND PROMOTION

With the proper information, a good marketing mix can be developed. One important decision is whether to alter the product and the promotion for the global marketplace. Other options are to radically change the product or to moderately adjust either the promotional message or the product to suit local conditions.

One Product, One Message

The strategy of global marketing standardization, which was discussed earlier, means developing a single product for all markets and promoting it the same way all over the world. For instance, Procter & Gamble uses the same product and promotional themes for Head and Shoulders in China as it does in the United States. The advertising draws attention to a person's dandruff problem, which stands out in a nation of black-haired people. Head and Shoulders is now the best-selling shampoo in China despite costing over 300 percent more than local brands. Buoyed by its success with Head and Shoulders, P&G is using the same product and same promotion strategy with Tide detergent in China. It also used another common promotion tactic that has been successful in the United States. The company spent half a million dollars to reach agreements with local washing machine manufacturers, which now include a free box of Tide with every new washer.

Other multinational firms are also applying uniform branding around the world on products such as Dove, Perrier, L'Oréal, and Hellmann's. Starbuck's faced a big obstacle in China. Coffee was traditionally so unpopular in China's tea-drinking culture until recently that many Starbucks didn't brew regular drip coffee until someone ordered it. Starbucks faced a dilemma: should they change their offerings to have more local appeal, or attempt to change Chinese tastes? Starbucks bet that a new generation of Chinese, with growing spending power and a desire for high status brands would try coffee. Coffee represents change from the old way of doing things. Once people enter a Chinese Starbucks, the education process begins. The chain stacks cream and sugar counters with brochures titled "Coffee Brewing Wisdom" and others that answer questions like "What is espresso?" Workers float through stores, passing out small cups of pumpkin-spice latte and other drinks.

Good-for-you messages about coffee are sometimes part of the pitch.[50] The process seems to be working. One of your authors recently visited a number of Starbucks in several cities and observed many young upscale Chinese in every one!

A recent survey asked 13,000 consumers in 20 countries about brand preferences across several product categories. Consumers in developing countries often viewed local products less favorably than global brands. Exhibit 5.6 reveals that Western brands fair quite well in the countries surveyed. The top cola brand in every country was either Pepsi or Coke.[51]

Global media—especially satellite and cable TV networks like CNN International, MTV Networks, and British Sky Broadcasting—make it possible to beam advertising to audiences unreachable a few years ago. Eighteen-year-olds in Paris often have more in common with 18-year-olds in New York than with their own parents. Almost all of MTV's advertisers run unified, English-language campaigns in the nations the firm reaches. The audiences buy the same products, go to the same movies, listen to the same music, and sip the same colas. Global advertising works on that simple premise. Although teens throughout the world prefer movies above all other forms of television programming, films are closely followed by music videos, stand-up comedy, and then sports.

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Global marketing standardization can sometimes backfire. Unchanged products may fail simply because of cultural factors. The game *Trivial Pursuit* failed in Japan. It seems that getting the answers wrong can be seen as a loss of face. Any type of war game tends to do very poorly in Germany, even though Germany is by far the world's biggest game-playing nation. A successful game in Germany has plenty of details and thick rulebooks.

Sometimes the desire for absolute standardization must give way to practical considerations and local market dynamics. For example, because of the feminine connotations of the word *diet,* the European version of Diet Coke is Coca-Cola Light. In France, its country of origin, the leading brand of yogurt is called Danone, whereas in the United States, it goes by its anglicized name, Dannon. Even if the brand name differs by market—as with Lay's potato chips, which are Sabritas in Mexico—a strong visual relationship may be created by uniform application of the brandmark and graphic elements on packaging.[52]

Product Invention

In the context of global marketing, product invention can be taken to mean either creating a new product for a market or drastically changing an existing product. For the Japanese market, Nabisco had to remove the cream filling from its Oreo cookies because Japanese children thought they were too sweet. Campbell's Soup invented a watercress and duck gizzard soup that sells well in China. It is also considering a cream of snake soup. Frito-Lay's most popular potato chip in Thailand is shrimp flavored. Popular ice cream flavors in Japan include pickled orchid, eel, fish, sea slug, whale meat, soft-shelled turtle, and cedar chips. McDonald's struggled in Japan until it added a shrimp burger to the menu. Pepsi succeeds in Japan with "limited edition" drinks that create buzz on YouTube and other sites. The most successful has been "Ice Cucumber;" bloggers are debating whether it tastes more like melon or cucumber. Another popular "limited edition" drink was a cinnamon-based beverage called "Pepsi Red."[53]

Whirlpool has launched what it bills as the world's cheapest automatic washer, with an eye on low-income consumers who thought they could never afford one. Whirlpool invested $30 million over 18 months to develop the washing machine in Brazil. But the Ideale (the machine's brand name) is a global project because it is also manufactured in China and India. The washer was launched first in Brazil and China (where its Chinese name means Super Hand-Washing Washer). It followed in India a few months later. Soon it will be marketed in other developing countries. The target retail price: $150 to $200. Just about a quarter of Brazilian households have an automatic washing machine, and penetration is only about 8 percent in China and 4.5 percent in India.[54]

Exhibit 5.6

Emerging Markets Like American Brands

Top Brands in Various Countries			
Argentina		**Saudi Arabia**	
Car:	Ford	Fast food:	McDonald's
Fast food:	McDonald's	Iced tea:	Lipton
Make-up:	Avon	Mobile phone:	Nokia
Mobile phone:	Sony	Packaged cheese:	Kraft
Motorcycle:	Honda	Salty snacks:	Lay's
TV:	Philips	TV:	Sony
Top cola brand:	Coca-Cola	Top cola brand:	Pepsi
China		**South Africa**	
Beer:	Budweiser	Car:	Toyota
Coffee (ready to drink):	Nestea	Designer clothing store:	Levi's
Fast food:	KFC	Fast food:	KFC
Mobile phone:	Panasonic	Lipstick:	Revlon
Soap:	Safeguard	Mobile phone:	Nokia
TV:	Sony	TV:	LG
Top cola brand:	Coca-Cola	Top cola brand:	Coca-Cola
Egypt		**Thailand**	
Designer clothing store:	Nike	Beer:	Heineken
Fuel:	Mobil	Car:	Toyota
Hotel:	Hilton, Sheraton	Convenience store:	7-Eleven
Make-up:	Avon	Moisturizer:	Nivea
Shampoo:	Pert Plus	Whiskey/Scotch:	Johnnie Walker
TV:	Toshiba	TV:	Sony
Top cola brand:	Pepsi	Top cola brand:	Pepsi
India		**Turkey**	
Conditioner:	Garnier	Car:	BMW
Fast food:	McDonald's	Cognac:	Remy Martin
Motor oil:	Castrol	Designer clothing store:	DKNY, Gucci
MP3 player:	Sony	Fast food:	McDonald's
Coffee (ready to drink):	Nescafé	Hotel:	Hilton
TV:	LG	Iced tea:	Lipton
Top cola brand:	Pepsi	Top cola brand:	Coca-Cola
Romania			
Car:	Mercedes	Shampoo:	Head and Shoulders
Fast food:	McDonald's	Whiskey/Scotch:	Jack Daniels
Lipstick:	Avon	Top cola brand:	Coca-Cola
MP3 player:	Sony		

SOURCE: Synovate, Chicago (2007) Used by permission of Aegis Group, plc.

Consumers in different countries use products differently. For example, in many countries, clothing is worn much longer between washings than in the United States, so a more durable fabric must be produced and marketed. For Peru, Goodyear developed a tire that contains a higher percentage of natural rubber and has better treads than tires manufactured elsewhere in order to handle the tough Peruvian driving conditions. Rubbermaid has sold millions of open-top wastebaskets in America; Europeans, picky about garbage peeking out of bins, want bins with tight lids that snap into place.

Product Adaptation

Another alternative for global marketers is to slightly alter a basic product to meet local conditions. Sometimes it is as simple as changing the package size. In India, Unilever sells single-use sachets of Sunsilk shampoo for 2 to 4 cents. Unilever's Rexona brand deodorant sticks sell for 16 cents and up. They are big hits in India, the Philippines, Bolivia, and Peru—where Unilever has grabbed 60 percent of the deodorant market. A nickel-size Vaseline package and a tube containing enough Close Up toothpaste for 20 brushings sell for about 8 cents each. In Nigeria, Unilever sells 3-inch-square packets of margarine that don't need refrigeration.[55]

Sometimes power sources and/or voltage must be changed on electronic products. It may be necessary, for example, to change the size and shape of the electrical plug. In other cases, the change may be a bit more radical. In India, people often lack reliable access to electricity or can't afford batteries. So, Freeplay Energy Group of London created a radio that is charged by cranking a handle.

One of the world's best at product adaptation is the Korean firm LG Electronics. Kimchi, made from fermented cabbage seasoned with garlic and chili, is served with most meals in Korea, but when it's stored inside a normal refrigerator, its pungent odor taints nearby foods. LG Electronics introduced the kimchi refrigerator, a product specifically designed to address the odor problem. Featuring a separate compartment that isolates smelly kimchi from other foods, the fridge gradually became a must-have in Korean homes.

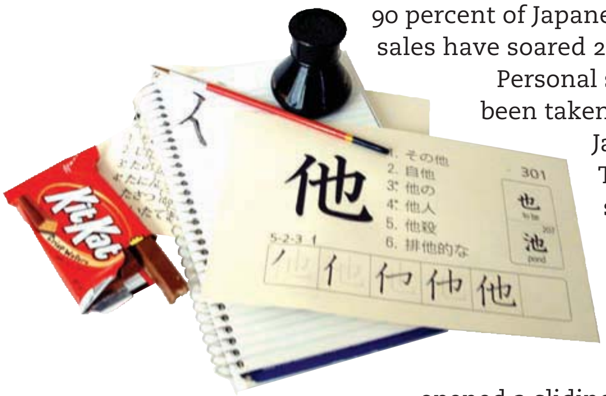
To meet the needs of Indian consumers, LG rolled out refrigerators with larger vegetable- and water-storage compartments, surge-resistant power supplies, and brightly colored finishes that reflect local preferences (red in the south, green in Kashmir). Saudi Arabians like LG's Primian refrigerator, which includes a special compartment for storing dates; the fruits, a Middle Eastern staple, spoil easily. For Saudis and other oil-rich consumers, LG has introduced a gold-plated 71-inch flat-screen television that sells for $80,000. In Iran, LG also offers a microwave oven with a preset button for reheating shish kebabs—a favorite dish.[56]

Promotion Adaptation

Another global marketing strategy is to maintain the same basic product but alter the promotional strategy. Bicycles are mainly pleasure vehicles in the United States. In many parts of the world, however, they are a family's main mode of transportation. Thus, promotion in these countries should stress durability and efficiency. In contrast, U.S. advertising may emphasize escape and fun.

Harley-Davidson decided that its American promotion theme, "One steady constant in an increasingly screwed-up world," wouldn't appeal to the Japanese market. The Japanese ads combine American images with traditional Japanese ones: American riders passing a geisha in a rickshaw, Japanese ponies nibbling at a Harley motorcycle. Waiting lists for Harleys in Japan are now six months long.

Kit Kat bars are a hit the world over, but Nestlé didn't have much luck selling them in Japan until it figured out how to crack the teen market. In Japan, the product's name is pronounced "kitto katsu," which roughly translates to "I hope you win." Fueling a rumor that Kit Kats bring success at crucial school exams, Nestlé rolled out packages combining the candy with other good-luck charms. Now



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90 percent of Japanese schoolkids say they've heard of Kit Kat bars, and Kit Kat sales have soared 28 percent.[57]

Personal selling is part of promotion, and nowhere has adaptation been taken so far as has Lexus in Japan. In the luxury car market in Japan, Lexus is over-shadowed by BMW and Mercedes Benz. To rectify that, Lexus hired a Japanese etiquette school that specialized in teaching the art of beautifying daily behavior. Now, when a Lexus salesperson opens a car door in a Lexus showroom for a potential customer, he or she points with all five fingers to the handle, right hand followed by left. Then, gracefully opens the door with both hands, in the same way Japanese samurais in the 14th century would have opened a sliding screen door.

At Lexus showrooms, sales consultants lean five to ten degrees forward and assume a warrior's "waiting position" when a customer is looking at a car. When serving customers coffee or tea, employees must kneel on the floor with both feet together and both knees on the ground. The coffee cup must never make a noise when it is placed on the table. All salespeople use a mirror to practice the "Lexus Face," a closed-mouth smile said to put customers at ease.[58]

Language barriers, translation problems, and cultural differences have generated numerous headaches for international marketing managers. Consider these examples:

- A toothpaste claiming to give users white teeth was especially inappropriate in many areas of Southeast Asia, where the well-to-do chew betel nuts and black teeth are a sign of higher social status.
- Procter & Gamble's Japanese advertising for Camay soap nearly devastated the product. In one commercial, a man meeting a woman for the first time immediately compared her skin to that of a fine porcelain doll. Although the ad had worked in other Asian countries, the man came across as rude and disrespectful in Japan.
- A teenager careening down a store aisle on a grocery cart in a Coca-Cola ad was perceived as too rebellious in Singapore.

PLACE (DISTRIBUTION)

Solving promotional and product problems does not guarantee global marketing success. The product still has to get adequate distribution. For example, Europeans don't play sports as much as Americans do, so they don't visit sporting-goods stores as often. Realizing this, Reebok started selling its shoes in nearly 800 traditional shoe stores in France. In one year, the company doubled its French sales. Harley-Davidson had to open two company-owned stores in Japan to get distribution for its Harley clothing and accessories.

The Japanese distribution system is considered the most complicated in the world. Imported goods wind their way through layers of agents, wholesalers, and retailers. For example, a bottle of 96 aspirins costs about $20 because the bottle passes through at least six wholesalers, each of whom increases the selling price. As a result, the Japanese consumer pays the world's most exorbitant prices. These distribution channels seem to be based on historical and traditional patterns of socially arranged trade-offs, which Japanese officials claim are very hard for the government to change. Today, however, the system appears to be changing because of pressure from Japanese consumers, who are attaching more importance to low prices in their purchasing decisions. The retailer who can cut distribution costs and therefore retail prices gets the sale. For example, Kojima, a Japanese electronics superstore chain like the U.S. chains Circuit City and Best Buy, had to bypass

General Electric's Japanese distribution partner Toshiba to import its merchandise at a good price. Toshiba's distribution system required refrigerators to pass through too many hands before they reached the retailer. Kojima went directly to GE headquarters in the United States and persuaded the company to sell it refrigerators, which were then shipped directly to Kojima. It now sells GE refrigerators for about $800—half the price of a typical Japanese model.

Innovative distribution systems can create a competitive advantage for savvy companies. Every day, dozens of flights touch down at Kenya's Nairobi Airport, unloading tourists. But when some of those same KLM and Kenya Airlines aircraft take off for the late-night trip home, they carry far more than weary travelers returning from African safaris. They're crammed with an average 25 tons apiece of fresh beans, bok choy, okra, and other produce harvested and packaged just the day before. It's all bound for eager—and growing—markets in Brussels, London, Paris, and other European cities.

Those flights are integral parts of an innovative supply chain. Vegpro Kenya, one of the nation's top produce exporters, operates seven farms within a two-hour drive of the airport. Every morning, trucks full of just-picked vegetables—30 varieties in all—dash to the airport. There, inside Vegpro's 27,000-square-foot air-conditioned cargo bay, more than 1,000 workers wash and sort the vegetables before they are rushed onto planes, ensuring that there's no break in the "cool chain" before the produce arrives in European stores the next day.

Companies are using creative strategies to combat distribution problems. Colgate-Palmolive introduced Indian villagers to the concept of brushing teeth by rolling into villages with video vans showing half-hour infomercials on the benefits of toothpaste. The company received more than half of its revenue in India from rural areas in 2006. Until recently, the rural market was virtually invisible, due to a lack of distribution. Unilever's Indian subsidiary, Hindustan Lever, sells its cosmetics, toothpastes, and detergents door-to-door. It now has over a million direct-sales consultants. In many developing nations, channels of distribution and the physical infrastructure are inadequate. In China, the main modes of transport are truck and train. But in a fragmented trucking industry with few major companies, multinationals have difficulty determining which companies are reliable. A lack of refrigerated trucks has meant that poultry giant Tyson Foods can only distribute in a handful of Chinese cities.[59] And the rail system is plagued by theft.

If China is bad, India is worse. Most Indian roads are simple two-lane affairs, maintained badly if at all. Shipping goods by rail costs twice as much on average as in developed countries and three times as much as in China. At India's ports, shipments often languish for days, waiting for customs clearance and loading berths; goods typically take 6 to 12 weeks to reach the United States, compared with 2 to 3 weeks for goods from China.[60]

In traffic-choked cities from Manila to Montevideo, McDonald's deploys fleets of motor scooters to get hot food to customers. All told, McDonald's delivers in some 31 cities. In 2007 the company launched deliveries in Taipei, with 1,000 drivers, and expanded Shanghai to citywide service. It is now testing the concept in Beirut and Riyadh. In Egypt, where the setup was pioneered in 1995, deliveries now account for 27 percent of all McDonald's revenue—up to 80 percent at some restaurants. Today, almost all of McDonald's 35 restaurants in and around Cairo deliver, while only a few have drive-through windows.[61]

American companies importing goods to the United States face other problems. Logistics has been a growing challenge for U.S. companies seeking to cut costs by shifting production to countries with cheaper manufacturing. Now, however, the rising cost of shipping goods increases their profit pressures. The recent surge in global trade has added to strains and charges for all forms of transport. As a result, some manufacturers are developing costly buffer stocks—which can mean setting up days' or weeks' worth of extra components—to avoid shutting down production lines and failing to make timely deliveries. Others are shifting to more reliable, but also more expensive, modes of transport, like airfreight, which is faster and less prone to delays than ocean shipping. Some companies are turning to new information technology to keep supply chains flowing and are hiring experts to help determine the best U.S. ports to use each week.

PRICING

Once marketing managers have determined a global product and promotion strategy, they can select the remainder of the marketing mix. Pricing presents some unique problems in the global sphere. Exporters must not only cover their production costs but also consider transportation costs, insurance, taxes, and tariffs. When deciding on a final price, marketers must also determine what customers are willing to spend on a particular product. And marketers need to ensure that their foreign buyers will pay that price. Because developing nations lack mass purchasing power, selling to them often poses special pricing problems. Sometimes a product can be simplified in order to lower its price. The firm must not assume that low-income countries are willing to accept lower quality, however. Although the nomads of the Sahara are very poor, they buy expensive fabrics to make their clothing. Their survival in harsh conditions and extreme temperatures requires this expense. Additionally, certain expensive luxury items can be sold almost anywhere. L'Oréal was unsuccessful selling cheap shampoo in India, so the company targets the rising class. It now sells a $17 Paris face powder and a $25 Vichy sunscreen. Both products are very popular.

Exchange Rates

The exchange rate is the price of one country's currency in terms of another country's currency. If a country's currency *appreciates*, less of that currency is needed to buy another country's currency. If a country's currency *depreciates*, more of that currency will be needed to buy another country's currency.

How do appreciation and depreciation affect the prices of a country's goods? If, say, the U.S. dollar depreciates relative to the Japanese yen, U.S. residents have to pay more dollars to buy Japanese goods. To illustrate, suppose the dollar price of a yen is $0.012 and that a Toyota is priced at 2 million yen. At this exchange rate, a U.S. resident pays $24,000 for a Toyota ($0.012 × 2 million yen = $24,000). If the dollar depreciates to $0.018 to one yen, then the U.S. resident will have to pay $36,000 for a Toyota.

As the dollar depreciates, the prices of Japanese goods rise for U.S. residents, so they buy fewer Japanese goods—thus, U.S. imports may decline. At the same time, as the dollar depreciates relative to the yen, the yen appreciates relative to the dollar. This means prices of U.S. goods fall for the Japanese, so they buy more U.S. goods—and U.S. exports rise.

floating exchange rates
Prices of different currencies move up and down based on the demand for and the supply of each currency.

dumping
The sale of an exported product at a price lower than that charged for the same or a like product in the "home" market of the exporter.

Currency markets primarily operate under a system of floating exchange rates. Prices of different currencies "float" up and down based on the demand for and the supply of each currency. Global currency traders create the supply of and demand for a particular country's currency based on that country's investment, trade potential, and economic strength.

Dumping

Dumping is the sale of an exported product at a price lower than that charged for the same or a like product in the "home" market of the exporter. This practice is regarded as a form of price discrimination that can potentially harm the importing nation's competing industries. Dumping may occur as a result of exporter business strategies that include (1) trying to increase an overseas market share, (2) temporarily distributing products in overseas markets to offset slack demand in the home market, (3) lowering unit costs by exploiting large-scale production, and (4) attempting to maintain stable prices during periods of exchange rate fluctuations.

Historically, the dumping of goods has presented serious problems in international trade. As a result, dumping has led to significant disagreements among countries and diverse views about its harmfulness. Some trade economists view dumping as harmful only when it involves the use of "predatory" practices that intentionally try to eliminate competition and gain monopoly power in a market. They believe that predatory dumping rarely occurs and that antidumping rules are a protectionist tool whose cost to consumers and import-dependent industries exceeds the benefits to the industries receiving protection.

Recently, the U.S. accused Vietnam of dumping textile products on the U.S. market. The U.S. imports about $4 billion worth of garments from Vietnam each year.[62] To date, the dumping claim has not been resolved.

Countertrade

countertrade
A form of trade in which all or part of the payment for goods or services is in the form of other goods or services.

Global trade does not always involve cash. Countertrade is a fast-growing way to conduct global business. In **countertrade**, all or part of the payment for goods or services is in the form of other goods or services. Countertrade is thus a form of barter (swapping goods for goods), an age-old practice whose origins have been traced back to cave dwellers. The U.S. Department of Commerce says that roughly 30 percent of all global trade is countertrade. In fact, both India and China have made billion-dollar government purchasing lists, with most of the goods to be paid for by countertrade. Recently, the Malaysian government bought 20 diesel-powered locomotives and paid for them with palm oil.

One common type of countertrade is straight barter. For example, PepsiCo sends Pepsi syrup to Russian bottling plants and in payment gets Stolichnaya vodka, which is then marketed in the West. Another form of countertrade is the compensation agreement. Typically, a company provides technology and equipment for a plant in a developing nation and agrees to take full or partial payment in goods produced by that plant. For example, General Tire Company supplied equipment and know-how for a Romanian truck tire plant. In turn, General Tire sold the tires it received from the plant in the United States under the Victoria brand name. Pierre Cardin gives technical advice to China in exchange for silk and cashmere. In these cases, both sides benefit even though they don't use cash.

REVIEW LEARNING OUTCOME

LO 5 List the basic elements involved in developing a global marketing mix

Global Marketing Mix

PRODUCT + PROMOTION	PLACE (Distribution)	PRICE
One Product, One Message	Channel Choice	Dumping
Product Invention	Channel Structure	Countertrade
Product Adaptation	Country Infrastructure	Exchange Rates
Message Adaptation		Purchasing Power

LO 6

The Impact of the Internet

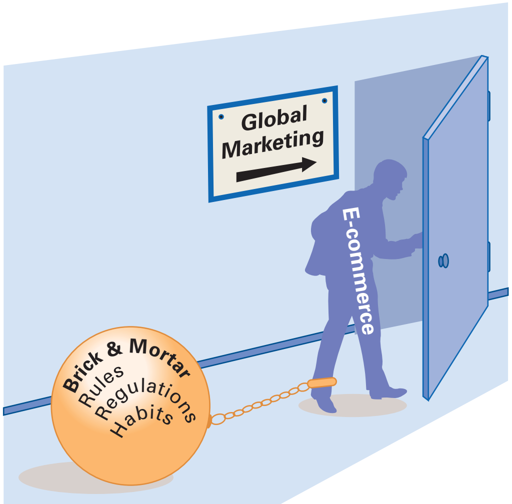
In many respects "going global" is easier than ever before. Opening an e-commerce site on the Internet immediately puts a company in the international marketplace. Sophisticated language translation software can make any site accessible to persons around the world. Global shippers like UPS, FedEx, and DHL help solve international e-commerce distribution complexities. E4X, Inc., offers software to ease currency conversions. Sites that use E4X's software can post prices in U.S. dollars, then ask their customers what currency they wish to use for payment. If the answer is a currency other than dollars, E4X takes over the transaction and translates the price into any of 22 currencies, collects the payment from the customer, and pays the site in dollars, just as though it were any other transaction. Customers never realize they're dealing with a third party.

Nevertheless, the promises of "borderless commerce" and the global "Internet economy" are still restrained by old brick-and-mortar rules, regulations, and habits. For example, Lands' End is not allowed to mention its unconditional refund policy on its e-commerce site in Germany because German retailers, who normally do not allow returns after 14 days, sued and won a court ruling blocking mention of it. Credit cards may be the currency of the Internet, but not everyone uses them. Americans spend an average of $6,500 per year by credit card, whereas Japanese spend less than $2,000. Many Japanese don't even have a credit card. So how do they pay for e-commerce purchases? 7-Eleven Japan, with over 8,000 convenience stores, has come to the rescue. eS-Books, the Japanese Web site partner of Yahoo! Japan, lets shoppers buy books and videos on the Internet, then specify to which 7-Eleven the merchandise is to be shipped. The buyer goes to that specific store and pays cash for the e-purchase.

Like the Japanese, Scandinavians are reluctant to use credit cards, and the French have an *horreur* of revealing the private information that Net retailers often request. French Web sites tend to be decidedly French. For example, FNAC, the largest French video, book, and music retailer, offers a daily "cultural newspaper" at its site. A trendy Web site in France will have a black background, while German shoppers prefer sites with bright colors and geometrical layouts. Dutch surfers are keen on video downloads, and Scandinavians appreciate images of nature.

REVIEW LEARNING OUTCOME

LO 6 Discover how the Internet is affecting global marketing



6 < number of regional Indian languages spoken in Pillsbury Doughboy advertisements

portion of industrial production exported by the U.S. > **1/5**

160 < number of countries in which Coca-Cola sells its products

weeks of vacation time legally required in France > **5**

450 million < number of cell phone users in China

number of days it takes to start a business in Mozambique > **153**

2 < number of days it takes to start a business in Canada

$6 trillion < combined economy of Canada, Mexico, and the U.S.

percentage of U.S. exports generated by small companies > **96**

400 < number of U.S. franchises with overseas locations

Review and Applications

LO 1 Discuss the importance of global marketing. Businesspeople who adopt a global vision are better able to identify global marketing opportunities, understand the nature of global networks, create effective global marketing strategies, and compete against foreign competition in domestic markets.

1.1 What is meant by "having a global vision"? Why is it important?

1.2 Isolationists have suggested that America would be much better off economically and politically if we just "built a wall" around the country and didn't deal with outsiders. Do you agree? Why or why not?

1.3 Discuss jobs outsourcing. Is it beneficial to U.S. firms?

LO 2 **Discuss the impact of multinational firms on the world economy.** Multinational corporations are international businesses that regularly operate across national borders. Because of their vast size and financial, technological, and material resources, multinational corporations have a great influence on the world economy. They have the ability to overcome trade problems, save on labor costs, and tap new technology. However, some countries are beginning to block foreign investment by multinationals.

2.1 Rubbermaid, the U.S. manufacturer of kitchen products and other household items, is considering moving to global marketing standardization. What are the pros and cons of this strategy?

2.2 Do you believe that multinationals are beneficial or harmful to developing nations? Why? What could foreign governments do to make them more beneficial?

LO 3 **Describe the external environment facing global marketers.** Global marketers face the same environmental factors as they do domestically: culture, economic and technological development, political structure and actions, demography, and natural resources. Cultural considerations include societal values, attitudes and beliefs, language, and customary business practices. A country's economic and technological status depends on its stage of industrial development, which, in turn, affects average family incomes. The political structure is shaped by political ideology and such policies as tariffs, quotas, boycotts, exchange controls, trade agreements, and market groupings. Demographic variables include the size of a population and its age and geographic distribution.

3.1 Many marketers now believe that teenagers in the developed countries are becoming "global consumers." That is, they all want and buy the same goods and services. Do you think this is true? If so, what has caused the phenomenon?

3.2 Renault and Peugeot dominate the French market but have no presence in the U.S. market. Why do you think that this is?

WRITING

3.3 Suppose that your state senator has asked you to contribute a brief article to her constituents' newsletter that answers the question, "Will there ever be a United States of Europe?" Write a draft of your article, and include reasons why or why not.

TEAM

3.4 Divide into six teams. Each team will be responsible for one of the following industries: entertainment; pharmaceuticals; computers and software; financial, legal, or accounting services; agriculture; and textiles and apparel. Interview one or more executives in each of these industries to determine how the WTO, NAFTA, and CAFTA have affected and will affect their organizations. If a local firm cannot be contacted in your industry, use the library and the Internet to prepare your report.

3.5 What are the major barriers to international trade? Explain how government policies can either restrict or stimulate global marketing.

LO 4 **Identify the various ways of entering the global marketplace.** Firms use the following strategies, in descending order of risk and profit, to enter global markets: direct investment, joint venture, contract manufacturing, licensing and franchising, and exporting.

4.1 Candartel, an upscale manufacturer of lamps and lampshades in America, has decided to "go global." Top management is having trouble deciding how to develop the market. What are some market entry options for the firm?

4.2 Explain how the U.S. Commercial Service can help companies wanting to enter the international market.

4.3 What are some of the advantages and potential disadvantages of entering a joint venture?

4.4 Why is direct investment considered risky?

LO 5 **List the basic elements involved in developing a global marketing mix.** A firm's major consideration is how much it will adjust the four Ps—product, promotion, place (distribution), and price—within each country. One strategy is to use one product and one promotion message worldwide. A second strategy is to create new products for global markets. A third strategy is to keep the product basically the same but alter the promotional message. A fourth strategy is to slightly alter the product to meet local conditions.

5.1 The sale of cigarettes in many developed countries either has peaked or is declining. However, the developing markets represent major growth markets. Should U.S. tobacco companies capitalize on this opportunity?

5.2 Describe at least three situations in which an American company might want to keep the product the same but alter the promotion. Also, give three examples in which the product must be altered.

5.3 Explain how exchange rates can affect a firm's global sales.

LO 6

Discover how the Internet is affecting global marketing. Simply creating a Web site can open the door for international sales. International carriers, like UPS, can help solve logistics problems. Language translation software can help an e-commerce business become multilingual. Yet cultural differences and old-line rules, regulations, and taxes hinder rapid development of e-commerce in many countries.

6.1 Describe how "going global" via the Internet presents opportunities and challenges.

6.2 Give several examples of how culture may hinder "going global" via the Internet.

Key Terms

buyer for export	144
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Exercises

APPLICATION EXERCISE

To be effective as a marketer, it is important to know geography. How will you be able to decide whether to expand into a new territory (domestic or foreign) if you don't know where it is and something about its culture, currency, and economy? If you can't place the European countries on a blank map, or if you can't label the lower 48 states without a list to help you, you're not alone. In one study, students incorrectly located over 50 percent of European countries and over 25 percent of the states in the Unites States. To help you brush up on your geography, we've compiled some tools that you may find useful.[63]

Activities

1. To review domestic geography, go to **http://www.50states.com/tools/usamap.htm** and print the blank map of the United States. Label the map. For a challenge, add the state capitals to the map.
2. Once you have successfully labeled the U.S. map, you may be ready to try labeling a world map. If so, go to **http://www.clickandlearn.com** and view the free, printable, blackline maps. Under the category of world maps, choose the blackline detail map. This shows country outlines, whereas the basic blackline outline map shows only the continents. You will notice that there are also blackline maps for each continent, so, if taking on the entire world is too daunting, start with more manageable blocks.

3. To be a global marketer, it is not enough to know where countries are located. You will need to know about the culture, the main exports, the currency, and even the main imports. Select a half-dozen or so countries with which you are unfamiliar, and research basic geographic information about them.

ETHICS EXERCISE

Moore Electronics sells automated lighting for airport runways. The government of an eastern European country has offered Moore a contract to provide equipment for the 15 major airports in the country. The official in charge of awarding the contract, however, is demanding a 5 percent kickback. He told Moore to build this into the contract price so that there would be no cost to Moore. Without the kickback, Moore loses the contract. Such kickbacks are considered a normal way of doing business in this country.

Questions

1. What should Moore do?
2. Review the Foreign Corrupt Practices Act online at http://www.usdoj.gov/criminal/fraud/fcpa/. Write a brief paragraph explaining how this statute relates to Moore's dilemma. Some American executives think this law causes American corporations to suffer a competitive disadvantage. Do you agree? Why or why not?

Case study: MTV


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ROCKING THE WORLD ONE NATION AT A TIME

To most people, MTV is as American as apple pie, baseball, and freedom of speech. It is a cultural icon to every American who grew up in the 1980s or 1990s, and it is easily one of the most palpable influences on the behavior of the demographic it targets with its programming. A closer look at MTV's business, however, reveals that its true significance is its ability to translate its formula for success into the many languages of the world. The network now owns 33 distinct channels that broadcast shows in 18 languages to 1.8 billion viewers in over 160 countries.

MTV Networks International, a subsidiary of MTV that actually dwarfs its parent, took its first steps on foreign soil with MTV Europe in 1987 and soon thereafter became Europe's largest television network. With a blueprint for success in hand, the large subsidiary turned its attention to the global youth market, which today includes over 2.5 billion people between the ages of 10 and 34. As it watched demand for television sets and paid programming services explode in rapidly developing markets, such as China, Latin America, and India, MTV was poised to capitalize.

Large and diverse markets, however, are difficult to understand and expensive to penetrate. Initially, MTV simply tried to export a standardized version of its American programming, but it quickly discovered that teens from around the world—much as they enjoy American music—are mostly interested in events in their own regions. MTV responded by undertaking the costly and complex task of producing localized content for specific markets. Now, veejay selection, programming, and service offerings are all unique in any given market.

Digital television and interactive services are very popular in Europe, so MTV UK developed a service that allows viewers to obtain information on CDs, check concert dates, and vote for their favorite performers during the MTV European Music Awards directly from their TV sets. In Asia, a virtual animated veejay named LiLi can interact with viewers in five different languages. Controlled by an actor behind the image, LiLi can also interview guests and provide popular culture tips. Brazilian viewers, who tend to be huge soccer fans, enjoy *Rockgol*, an MTV-produced soccer championship that has been opposed by Brazilian record industry executives and musicians.

MTV Japan, a joint venture between MTV Networks and local investment firm H&Q Asia Pacific, operates in the world's second largest music market and one of the world's most advanced mobile telecommunications markets. Identifying those two trends, MTV Japan developed a service that lets subscribers use their mobile phones to download entertainment news and new music or vote for their favorite veejay.

The development cycle is long for such detailed international projects, but MTV Networks International president Bill Roedy is a patient man. He spent ten years working with Chinese officials for the right to air MTV programming for just six hours a day. The payoff? Forty cable providers now carry MTV Mandarin into 60 million Chinese homes. Roedy is also sensitive to foreign leaders' fears that their culture will be "Americanized" by MTV. Before his networks enter markets with extreme cultural differences, such as Israel, Singapore, Cuba, or China, Roedy meets with key political figures to allay their fears. "We've had very little resistance once we explain that we're not in the business of exporting American culture," he notes.[64]

Questions

1. Identify the key environmental challenges MTV has faced in its effort to expand globally, and discuss how MTV has overcome them.
2. What is MTV's global market entry strategy? Discuss whether you agree with MTV's approach, and identify its advantages and disadvantages.
3. Discuss MTV's global product strategy.

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Company Clips

METHOD—GLOBAL BEGINNINGS

In the twenty-first century, startups can become global businesses much faster than in anytime in history. So, while new companies are forging their way domestically, they may also experience an added layer of challenges from trying to enter global markets at the same time. In this final video segment on method, founder Eric Ryan and CEO Alastair Dorward describe their company's perspective on global expansion and which foreign markets represent good opportunities for method.

Questions

1. Is method a multinational company? Explain.
2. Which environmental factors facing all global marketers is method confronting as it begins to expand into foreign markets?
3. Outline method's global marketing mix.
4. What is innovative about how method envisions moving into foreign markets? Would method's strategy for global expansion work for other companies or industries? Which ones? Explain.

Marketing & You Results

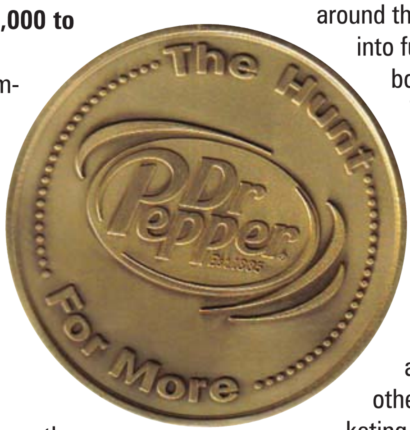
This questionnaire measures cultural openness. The higher your score, the more interested you are in learning about other cultures and interacting with people from other countries. People with high cultural openness tend to be less ethnocentric and more open to buying imported products than people with low cultural openness. As you read in Chapter 5, cultural openness is an important aspect of developing a global vision.

Marketing Miscues

Dr. Pepper Receives Chilly Welcome in Boston

Dr. Pepper-maker Cadbury Schweppes PLC decided to create the "Hunt for More" marketing promotion in which gold coins were hidden in 23 cities across the United States. Codes were placed on specially marked 24-ounce bottles and 24-packs of Dr. Pepper. Consumers could then obtain clues to the coin locations by entering these codes at DrPepper.com. Promotion contestants followed these geography, history, and world events-related clues as they were released in the hopes of winning the coin worth $1 million. The other 22 coins were worth anywhere from $10,000 to $250,000.

Clues to treasures were tied to a consumer's geographic region, based on the zip code used at registration. The final clue for the Boston area hunt was, "You're hot on the trail, though the place may feel chilly. The coin rests by the name of a patriot at rest in Philly." This clue sent contestants to the Granary Burial Ground on the Freedom Trail in Boston, an almost 350-year old graveyard where historic figures such as John Hancock, Paul Revere, Robert Treat Paine, and Samuel Adams are buried. However, the burial ground was closed and locked due to icy conditions, making it impossible for the treasure hunters to get inside to search for the coin. The city then refused to open the gates since city officials feared that mobs of treasure hunters would desecrate the sacred site. Additionally, any damage to the historic site could have resulted in felony charges against individuals in the hunt.



Apparently, the prized coin had been left in the cemetery earlier that day when the park was open. A Boston-area person working for Promotion Watch (a marketing company in Michigan) had hidden the coin, tucked in a black leather pouch, under a stone at the crypt for Edward and William Reynolds. According to this person, both he and Promotion Watch had objected to the hiding of the coin in the Granary, but that the other marketing company involved in the treasure hunt promotion, Circle One Marketing of Connecticut, ignored their concerns. Cadbury Schweppes took full responsibility for the campaign and responded quickly by canceling the Boston portion of the treasure hunt and issuing an apology to the city and the contestants. Additionally, the company offered to pay the costs of extra burial ground security after the clue announcement and made a $10,000 donation to the cemetery. As for the contestants, the company held a drawing among the contestants for the $10,000 prize, which was the value of the hidden coin. The $1 million coin was found in the Sam Houston Park in Texas near the Spirit of Confederacy statue.

The Dr. Pepper promotion happened to come on the heels of another unconventional marketing campaign gone bad. Only a month before, Boston had virtually shut down due to a guerrilla marketing campaign for Cartoon Network, Turner Broadcasting, in which city officials had feared terrorist attacks. In this campaign, light boxes featuring characters from the Aqua Teen Hunger Force were placed around the city. Boston city officials quickly went into full-scale emergency alert as the light boxes were mistaken for explosive devices. The fallout from the Aqua Teen Hunger Force marketing effort was much more severe than that of Dr. Pepper, as the two men who placed the devices throughout the city faced criminal charges. Additionally, the Cartoon Network chief ultimately resigned.

Cadbury Schweppes did not receive any complaints from city officials in the other 22 cities involved in the guerrilla marketing campaign. Interestingly, Turner Broadcasting had placed the Aqua Teen Hunger Force light devices in numerous other cities (Los Angeles, Chicago, Atlanta, Seattle, San Francisco, and Philadelphia) without any backlash from city officials. While many Boston city officials referred to such marketing efforts as intolerable and irresponsible, Boston's mayor, Thomas M. Menino, said that the city would not ban unconventional marketing schemes. However, he cautioned that companies had to notify city hall in advance about such plans.

Questions

1. Do marketers violate the ethos of social responsibility in guerilla marketing campaigns such as this? Why/why not?
2. Was the controversy a positive or a negative for Cadbury Schweppes?

Critical Thinking Case

Cannondale Bicycle—"Feel It"

Cannondale Bicycle Corporation began in 1971 with the introduction of the cycling industry's first bicycle trailer. The company's first bicycle, a touring model, was introduced in 1983, followed quickly in 1984 by a road racing model and a mountain bike model. Today, Cannondale is the leading manufacturer of high-end bicycles, selling more than 100 models in over 70 countries worldwide. The company's mission is to "create innovative, quality products that inspire cyclists around the world." As such, the company focuses on performance, innovation, and superiority in its product offerings, answering two major questions: (1) Does this innovation contribute to the ride? (2) Does it do what we want it to do? The philosophy is that the rider will "feel it" in the ride.

Cannondale is owned by Dorel Industries, Inc, a global consumer products company with headquarters in Montreal, Canada. Cannondale's worldwide headquarters is in Bethel, Connecticut. The company's bicycles are designed, developed, and produced primarily at its factory in Bedford, Pennsylvania. The company operates subsidiaries in Holland, Japan, and Australia.

Cannondale's heritage is in competitive cycling. The company sponsors the Vredestein/Cannondale mountain bike team and the Liquigas pro tour road racing teams, as well as select regional teams. The company's mountain bikes have captured 11 World Championships, 17 World Cup Series overall titles, 16 National Championships, and two Olympic medals. The company's road racing bikes have won 11 stages of the Tour de France, 27 stages of the Giro d'Italia, two Giro d'Italia overall victories, a Professional World Championship title, and two Italian National Championships. Cannondale's handcrafted bicycles have also won numerous design awards, including the "Publisher's Award for Innovation" from *Bicycling* magazine, "Technological Development of the Year Award" from *VeloNews* magazine, "Best of What's New" award from *Popular Science*, "Best New Products of the Year Award" from *Business Week*, "Design Production Award" from *ID* magazine, "Computer-Aided Design Award" from *Design News* magazine, and a "Design and Engineering Award" from *Popular Mechanics*.

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While Cannondale has long focused on product innovation related to its end-users, it realizes that retailers are customers too and is bringing its process innovation to the forefront of its customer service. In 2007, the company expanded its resource offerings for the retailers via **www.CannondaleStation.com**. The Web site educates, informs, and entertains its retailers while providing them in-depth product knowledge. There are five components of this dealer-only website. The LAB focuses on product education in a tutorial learning format with knowledge-retention certification quizzes. On The CRIT, dealers can submit product orders 24/7. The LINK provides sales support tools, marketing news, and technical information and updates. Assisting retailers in their promotional efforts is The HUB, with its thumbnail images for downloading. Finally, The BARN offers a site for the Cannondale community (e.g., riders, engineers, fans) to come together and share videos, photos, blogs, podcasts, and testimonials. Other bicycle manufacturers, such as Thule and Trek, also offer retailer-specific Web sites.

According to the National Sporting Goods Association, the number of people riding bicycles is decreasing. In 1996, 53.3 million Americans over seven years of age rode a bike at least six times year. That number dropped to 43.1 million in 2005 and to 35.6 million in 2006. Bike sales in the United States have been flat, suspended between $5.5 billion and $5.9 billion between 1999 and 2007. Research conducted by IDEO, a Palo Alto-based innovation/design consultancy group, found that American consumers are intimidated by bike riding, seeing it as a sport for hard-core athletes. Not surprisingly, these same former bicycle riders do not even like going into bicycle stores since they are also intimidated by the shopping experience itself. Apparently, there is a large group of consumers who do not "feel it" when it comes to the cycling marketplace.

Questions:

1. Describe the current and potential marketplaces for Cannondale Bicycle Corporation.
2. Describe Cannondale's marketing mix.

ANATOMY OF A Multinational Company

Starbucks

Starbucks has coffee shops in 27 different countries.

Strategic Fit

Starbucks chooses locations with shared values and strategic fit.

Australia, Austria, Beijing, Brazil, Canada, China, Czech Republic, France, Germany, Greece, Hawaii, Hong Kong, Ireland, Japan, Malaysia, Mexico, New Zealand, Peru, Shanghai, Singapore, South Korea, Spain, Switzerland, Taiwan, Thailand, Turkey, United Kingdom

(AP Photo/Moises Castillo)

Local Culture

Adapting to local culture helps maintain global business.

Familiar logo

Familiar logo ensures global marketing standardization.

Customer Experience

Starbucks maintains control of its customer experience through joint ventures and company-owned operations.

PART 2

Analyzing Marketing Opportunities

WHAT'S INSIDE

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CHAPTER 6 Consumer Decision Making

Learning Outcomes

- **LO 1** Explain why marketing managers should understand consumer behavior
- **LO 2** Analyze the components of the consumer decision-making process
- **LO 3** Explain the consumer's postpurchase evaluation process
- **LO 4** Identify the types of consumer buying decisions and discuss the significance of consumer involvement
- **LO 5** Identify and understand the cultural factors that affect consumer buying decisions
- **LO 6** Identify and understand the social factors that affect consumer buying decisions
- **LO 7** Identify and understand the individual factors that affect consumer buying decisions
- **LO 8** Identify and understand the psychological factors that affect consumer buying decisions

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LO 1

The Importance of Understanding Consumer Behavior

Consumers' product and service preferences are constantly changing. In order to address this constant state of flux and to create a proper marketing mix for a well-defined market, marketing managers must have a thorough knowledge of consumer behavior. **Consumer behavior** describes how consumers make purchase decisions and how they use and dispose of the purchased goods or services. The study of consumer behavior also includes an analysis of factors that influence purchase decisions and product use.

Understanding how consumers make purchase decisions can help marketing managers in several ways. For example, if a manager knows through research that gas mileage is the most important attribute for a certain target market, the manufacturer can redesign the product to meet that criterion. If the firm cannot change the design in the short run, it can use promotion in an effort to change consumers' decision-making criteria.

consumer behavior
Processes a consumer uses to make purchase decisions, as well as to use and dispose of purchased goods or services; also includes factors that influence purchase decisions and product use.

consumer decision-making process
A five-step process used by consumers when buying goods or services.

Marketing & You

What is your buying behavior?

Using the scales below, enter your answers.

1 2 3 4 5
Very often — Sometimes — Never

— I have felt others would be horrified if they knew of my spending habits.

— I've bought things even though I couldn't afford them.

— I've written a check when I knew I didn't have enough money in the bank to cover it.

— I've bought myself something in order to make myself feel better

— I've felt anxious or nervous on days I didn't go shopping.

— I've made only the minimum payments on my credit cards.

1 2 3 4 5
Strongly agree — Strongly disagree

— If I have any money left at the end of the pay period, I just have to spend it.

— Having more money would solve my problems.

— I have bought and arrived home not knowing why I had bought it.

Now, total your score. Read the chapter and find out what your score means at the end.

From Scale #98, Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds., Vol. III. © by American Marketing Association. Used with the permission of the American Marketing Association.

REVIEW LEARNING OUTCOME

LO 1 Explain why marketing managers should understand consumer behavior

Consumer behavior = HOW
- consumers make purchase decisions
- consumers use and dispose of products

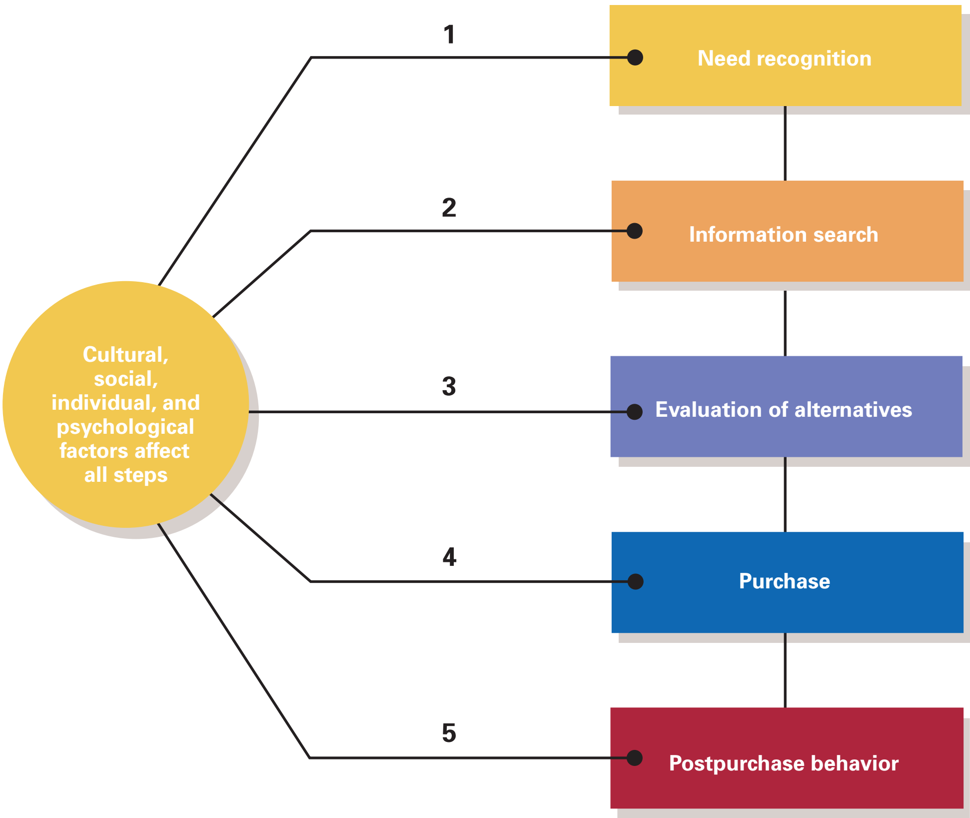
LO 2

The Consumer Decision-Making Process

When buying products, consumers generally follow the consumer decision-making process shown in Exhibit 6.1: (1) need recognition, (2) information search, (3) evaluation of alternatives, (4) purchase, and (5) postpurchase behavior. These five steps represent a general process that can be used as a guide for studying how consumers make decisions. It is important to

Exhibit 6.1

Consumer Decision-Making Process



note, though, that consumers' decisions do not always proceed in order through all of these steps. In fact, the consumer may end the process at any time or may not even make a purchase. The section on the types of consumer buying decisions later in the chapter discusses why a consumer's progression through these steps may vary. Before addressing this issue, however, we will describe each step in the process in greater detail.

NEED RECOGNITION

need recognition
Result of an imbalance between actual and desired states.

stimulus
Any unit of input affecting one or more of the five senses: sight, smell, taste, touch, hearing.

want
Recognition of an unfulfilled need and a product that will satisfy it.

The first stage in the consumer decision-making process is need recognition. **Need recognition** occurs when consumers are faced with an imbalance between actual and desired states. For example, have you ever gotten blisters from an old running shoe? Or maybe you have seen a TV commercial for a new sports car and wanted to buy it. Need recognition is triggered when a consumer is exposed to either an internal or an external **stimulus**. *Internal stimuli* are occurrences you experience, such as hunger or thirst. For example, you may hear your stomach growl and then realize that you are hungry. *External stimuli* are influences from an outside source such as someone's recommendation of a new restaurant, the color of an automobile, the design of a package, a brand name mentioned by a friend, or an advertisement on television or radio.

A marketing manager's objective is to get consumers to recognize an imbalance between their present status and their preferred state. Advertising and sales promotion often provide this stimulus. Surveying buyer preferences provides marketers with information about consumer wants and needs that can be used to tailor products and services. Marketing managers can create wants on the part of the consumer. A **want** exists when someone has an unfulfilled need and has determined that a particular good or service will satisfy it. For example, when college students move in to their own apartments or dorm rooms, they often need to furnish them and want new furniture rather than hand-me-downs from their parents. A want can be for a specific product, or it can be for a certain attribute or feature of a product. In this example, college students not only need home furnishings, but also want items that reflect their personal sense of style. Similarly, consumers may want ready-to-eat meals, drive-through dry-cleaning service, and Internet shopping to fill their need for convenience.

Another way marketers create new products and services is by observing trends in the marketplace. IKEA, the home furnishing giant, watches home decor trends and then creates affordable, trendy furniture. For example, marketers at IKEA realized that Generation Y consumers prefer furniture that is stylish, easy to clean, multifunctional, and portable. As a result, IKEA uses "bold orange, pink and green colors." The wood boasts a lacquered finish that can be wiped clean and doesn't need polish. IKEA also offers a space-saving, multifunction desk that converts into a dining table; it has wheels so that it can be easily moved.[1]

Consumers recognize unfulfilled wants in various ways. The two most common occur when a current product isn't performing properly and when the consumer is about to run out of something that is generally kept on hand. Consumers may also recognize unfulfilled wants if they become aware of a product that seems superior to the one currently used. Such wants are usually created by advertising and other promotional activities. For example, aware of the popularity of MP3s and consumers' desire to take their music with them, car stereo manufacturers such as Sonicblue and Kenwood have added MP3 interfaces. Other companies, including Apple, Microsoft, RCA, and Creative Technology, are hoping to fulfill consumer desires for smaller audio and video players, known as portable media centers. The newest devices have wireless Internet connection capabilities providing access to downloadable movies and TV as well as music and video games. But Apple continues to lead the field with its iPod Shuffle and Nano and extensive downloadable music and TV programs.[2]

Marketers selling their products in global markets must carefully observe the needs and wants of consumers in various regions. Unilever hit on an unrecognized need of European consumers when it introduced Persil Tablets, premeasured laundry detergent in tablet form. Though the tablets are more expensive than regular detergents, Unilever found that European consumers considered laundry a chore and wanted the process to be as simple and uncomplicated as possible. Unilever launched the tablets as a less messy and more convenient alternative. The laundry tablets were an immediate success in the United Kingdom and enabled Unilever's Persil brand to beat out rival Procter & Gamble's best-selling Ariel powder detergent.[3]

INFORMATION SEARCH

After recognizing a need or want, consumers search for information about the various alternatives available to satisfy it. For example, as gasoline prices increase, many people are searching for information on vehicles fueled by alternative means such as Honda's hybrid models. An information search can occur internally, externally, or both. In an internal information search, the person recalls information stored in the memory. This stored information stems largely from previous experience with a product. For example, while traveling with your family, you encounter a hotel where you stayed during spring break earlier that year. By searching your memory, you can probably remember whether the hotel had clean rooms and friendly service.

internal information search
The process of recalling past information stored in the memory.

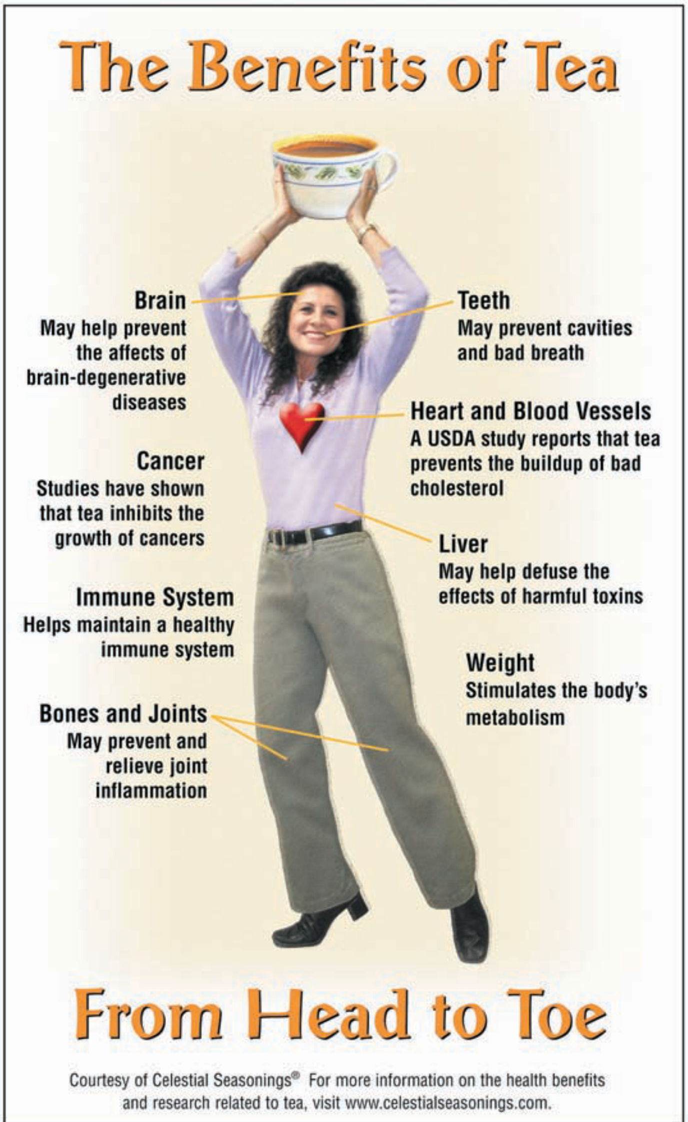
external information search
The process of seeking information in the outside environment.

nonmarketing-controlled information source
A product information source that is not associated with advertising or promotion.

In contrast, an external information search seeks information in the outside environment. There are two basic types of external information sources: nonmarketing-controlled and marketing-controlled. A nonmarketing-controlled information source is not associated with marketers promoting a product. These information sources include personal experiences (trying or observing a new product); personal sources (family, friends, acquaintances, and coworkers who may recommend a product or service); and public sources, such as Underwriters Laboratories, *Consumer Reports*, and other rating organizations that comment on products and services. For example, if you are in the mood to go to the movies, you may search your memory for past experiences at various cinemas when determining which one to go to (personal experience). To choose which movie you will see, you may rely on the recommendation of a friend or family member (personal sources). Alternatively, you may read the critical reviews in the newspaper or online (public sources). Marketers gather information on how these information sources work and use it to attract customers. For example, car manufacturers know that younger customers are likely to get information from friends and family, so they try to develop enthusiasm for their products via word of mouth.

marketing-controlled information source
A product information source that originates with marketers promoting the product.

On the other hand, a **marketing-controlled information source** is biased toward a specific product because it originates with marketers promoting that product. Marketing-controlled information sources include mass-media advertising (radio, newspaper, television, and magazine advertising), sales promotion (contests, displays, premiums, and so forth), salespeople, product labels and packaging, and the Internet. Many consumers, however, are wary of the information they receive from marketing-controlled sources, believing that most marketing campaigns stress products' attributes and ignore their faults. These sentiments tend to be stronger among better educated and higher-income consumers. Some marketing-controlled information sources can shift out of marketers' control, however, when there is bad news to report. Toy maker, Mattel Inc., has lately made headlines for its recall of toys with lead paint contamination and powerful magnets that can cause illness or even death if children ingest them. Newspaper stories across the country, in this instance a nonmarketing-controlled information source, recounted the many toy recalls Mattel has had to make in the past. Mattel then used marketing-controlled information sources to try to combat the negative publicity. Damage control for Mattel took the form of full-page ads in *The New York Times* and *The Wall Street Journal*, as well as video coverage on its own and Yahoo's Web sites, with an apology and assurances of future safety of its products from Bob Eckert, Mattel's chairman and CEO.



Whereas nonmarketing controlled information is neutral, marketing-controlled information is biased toward a specific product. This ad from Celestial Seasonings seems to cut through both types: it proclaims the benefits of tea in general, but since the company name is on the ad as a sponsor, the information cannot be considered completely unbiased. Or can it?

The extent to which an individual conducts an external search depends on his or her perceived risk, knowledge, prior experience, and level of interest in the good or service. Generally, as the perceived risk of the purchase increases, the consumer enlarges the search and considers more alternative brands. For example, suppose that you want to purchase a surround sound system for your home stereo. The decision is relatively risky because of the expense and technical nature of the stereo system, so you are motivated to search for information about models, prices, options, compatibility with existing entertainment products, and capabilities. You may decide to compare attributes of many speaker systems because the value of the time expended finding the "right" stereo will be less than the cost of buying the wrong system.

A consumer's knowledge about the product or service will also affect the extent of an external information search. A consumer who is knowledgeable and well informed about a potential purchase is less likely to search for additional information. In addition, the more knowledgeable consumers are, the more efficiently they will conduct the search process, reducing their required search time. For example, many consumers know that AirTran and other discount airlines have much lower fares, so they routinely use the discounters without even checking fares at other airlines.

The extent of a consumer's external search is also affected by confidence in one's decision-making ability. A confident consumer not only has sufficient stored information about the product, but also feels self-assured about making the right decision. People lacking this confidence will continue an information search even when they know a great deal about the product. Consumers with prior experience in buying a certain product will have less perceived risk than inexperienced consumers. Therefore, they will spend less time searching and limit the number of products that they consider.

A third factor influencing the external information search is product experience. Consumers who have had a positive prior experience with a product are more likely to limit their search to items related to the positive experience. For example, when flying, consumers are likely to choose airlines with which they have had positive experiences, like consistent on-time arrivals. They will avoid airlines with which they have had a negative experience, such as lost luggage.

Finally, the extent of the search is positively related to the amount of interest a consumer has in a product. A consumer who is more interested in a product will spend more time searching for information and alternatives. For example, suppose you need a new pair of running shoes. If you are a dedicated runner who reads jogging and fitness magazines and catalogs, you may enjoy reading about the new brands available and spend more time and effort than other buyers in deciding on the right shoe.

evoked set (consideration set) A group of brands, resulting from an information search, from which a buyer can choose.

The consumer's information search should yield a group of brands, sometimes called the buyer's evoked set (or consideration set), which are the consumer's most preferred alternatives. From this set, the buyer will further evaluate the alternatives and make a choice. Consumers do not consider all brands available in a product category, but they do seriously consider a much smaller set. For example, from the many brands of pizza available, consumers are likely to consider only the alternatives that fit their price range, location, take-out/delivery needs, and taste preferences. Having too many choices can actually confuse consumers and slow their decision making, or even completely deter them from buying a product.

EVALUATION OF ALTERNATIVES AND PURCHASE

After getting information and constructing an evoked set of alternative products, the consumer is ready to make a decision. A consumer will use the information stored in memory and obtained from outside sources to develop a set of criteria. These standards help the consumer evaluate and compare alternatives. One way to begin narrowing the number of choices in the evoked set is to pick a product attribute and then exclude all products in the set that don't have that attribute. For example, assume Jane and Jill, both college sophomores, are looking for their first apartment. They need a two-bedroom apartment, reasonably priced, and located near campus. They want the apartment to have a swimming pool, washer and dryer, and covered parking. Jane and Jill begin their search with all apartments in the area and then systematically eliminate possibilities that lack the features they need. Hence, if there are 50 options in the area, they may reduce their list to just 10 apartments that possess all of the desired attributes.

Another way to narrow the number of choices is to use cutoffs. Cutoffs are either minimum or maximum levels of an attribute that an alternative must pass to be considered. Suppose Jane and Jill set a maximum of $1,000 to spend on combined rent. Then all apartments with rent higher than $1,000 will be eliminated, further reducing the list of apartments from ten to eight. A final way to narrow the choices is to rank the attributes under consideration in order of importance and evaluate the products based on how well each performs on the most important attributes. To reach a final decision on one of the remaining eight apartments, Jane and Jill may decide proximity to campus is the most important attribute. As a result, they will choose to rent the apartment closest to campus.

If new brands are added to an evoked set, the consumer's evaluation of the existing brands in that set changes. As a result, certain brands in the original set may become more desirable. Suppose Jane and Jill find two apartments located equal distances from campus, one priced at $800 and the other at $750. Faced with this choice, they may decide that the $800 apartment is too expensive given that a comparable apartment is cheaper. If they add a $900 apartment to the list, however, then they may perceive the $800 apartment as more reasonable and decide to rent it.

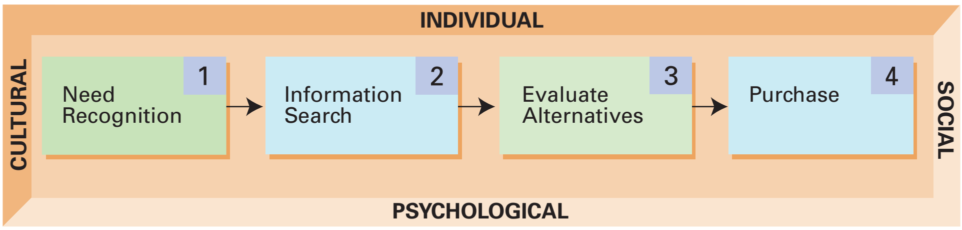
The goal of the marketing manager is to determine which attributes have the most influence on a consumer's choice. Several attributes may collectively affect a consumer's evaluation of products. A single attribute, such as price, may not adequately explain how consumers form their evoked set. Moreover, attributes the marketer thinks are important may not be very important to the consumer. For example, if you are buying a laptop computer or iBook, you will first have to determine which computers are in your price range. But, in making a final decision, you may also consider weight, screen size, software included, processor speeds, CD and DVD drives, service packages, and reputation.

Economic issues and concerns can also have a significant impact on a consumer's ultimate choice. A 2006 survey found that households earning as much as $75,000 a year have begun changing their spending habits in response to rising fuel prices and slow-downs in the housing market. Items most likely to be thrown out of the evoked set: fashion accessories, clothing, home décor, electronics, and entertainment. Middle-income shoppers are being more deliberate about when—and how often— to trade up to a high-end item.[4]

Following the evaluation of alternatives, the consumer decides which product to buy or decides not to buy a product at all. If he or she does make a purchase, the next step in the process is an evaluation of the product after the purchase.

REVIEW LEARNING OUTCOME

LO 2 Analyze the components of the consumer decision-making process



LO 3
Postpurchase Behavior

When buying products, consumers expect certain outcomes from the purchase. How well these expectations are met determines whether the consumer is satisfied or dissatisfied with the purchase. For example, if a person bids on a used car stereo from eBay and wins, he may have fairly low expectations regarding performance. If the stereo's performance turns out to be of superior quality, then the person's satisfaction will be high because his expectations were exceeded. Conversely, if he bid on a new car stereo expecting superior quality and performance, but the stereo broke within one month, he would be very dissatisfied because the product failed to meet his expectations. Price often influences the level of expectations for a product or service.

For the marketer, an important element of any postpurchase evaluation is reducing any lingering doubts that the decision was sound. When people recognize inconsistency between their values or opinions and their behavior, they tend to feel an inner tension called **cognitive dissonance.** For example, suppose a person who normally tans in a tanning bed decides to try a new "airbrush" tanning method, called a "Hollywood" or "mystic" tanning. Mystic tanning costs $30 to $50, significantly more than "fake tanner" or a tanning bed. Prior to spending more on the tan, she may feel inner tension or anxiety, which is a feeling of dissonance. This feeling occurs because she knows the product has some disadvantages, such as being expensive, and some advantages, like being free of harmful ultraviolet rays. In this case, the disadvantage of higher cost battles the advantage of avoiding harmful UV rays.[5]

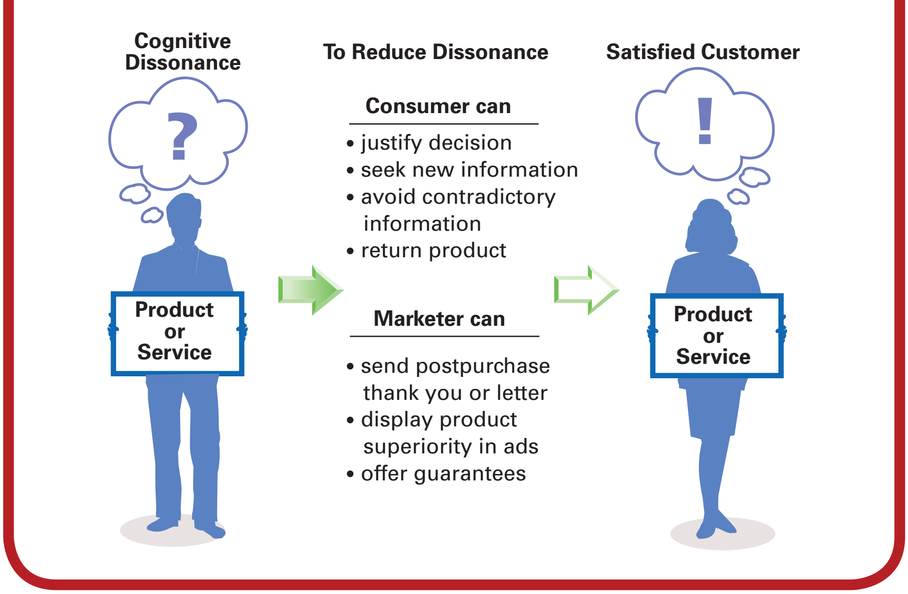
cognitive dissonance
Inner tension that a consumer experiences after recognizing an inconsistency between behavior and values or opinions.

Consumers try to reduce dissonance by justifying their decision. They may seek new information that reinforces positive ideas about the purchase, avoid information that contradicts their decision, or revoke the original decision by returning the product. To ensure satisfaction, thereby reducing dissonance, consumers using the "mystic tanning" mentioned above may ask several friends about their experiences, do online research, and talk with the tanning booth representative to obtain additional information about the procedure. In some instances, people deliberately seek contrary information in order to refute it and reduce dissonance. Dissatisfied customers sometimes rely on word of mouth to reduce cognitive dissonance by letting friends and family know they are displeased.

Marketing managers can help reduce dissonance through effective communication with purchasers. For example, a customer service manager may slip a note inside the package congratulating the buyer on making a wise decision. Postpurchase letters sent by manufacturers and dissonance-reducing statements in instruction booklets may help customers feel at ease with their purchase. Advertising that displays the product's superiority over competing brands or guarantees can also help relieve the possible dissonance of someone who has already bought the product. In the tanning example, the tanning salon may offer a 100 percent money-back guarantee. The **mystictan.com** Web site explains the procedure and even shows endorsements from various celebrities.[6] Because the company offers this additional information and communicates effectively with its customers, they are more likely to understand the procedure and the expected results; hence, it is likely that the outcome will meet or exceed their expectations instead of disappointing them.

REVIEW LEARNING OUTCOME

LO3 Explain the consumer's postpurchase evaluation process



LO4

Types of Consumer Buying Decisions and Consumer Involvement

All consumer buying decisions generally fall along a continuum of three broad categories: routine response behavior, limited decision making, and extensive decision making (see Exhibit 6.2). Goods and services in these three categories can best be described in terms of five factors: level of consumer involvement, length of time to make a decision, cost of the good or service, degree of information search, and the number of alternatives considered. The level of consumer involvement is perhaps the most significant determinant in classifying buying decisions. **Involvement** is the amount of time and effort a buyer invests in the search, evaluation, and decision processes of consumer behavior.

involvement
The amount of time and effort a buyer invests in the search, evaluation, and decision processes of consumer behavior.

routine response behavior
The type of decision making exhibited by consumers buying frequently purchased, low-cost goods and services; requires little search and decision time.

limited decision making
The type of decision making that requires a moderate amount of time for gathering information and deliberating about an unfamiliar brand in a familiar product category.

extensive decision making
The most complex type of consumer decision making, used when buying an unfamiliar, expensive product or an infrequently bought item; requires use of several criteria for evaluating options and much time for seeking information.

Frequently purchased, low-cost goods and services are generally associated with **routine response behavior**. These goods and services can also be called low-involvement products because consumers spend little time on search and decision before making the purchase. Usually, buyers are familiar with several different brands in the product category but stick with one brand. Consumers engaged in routine response behavior normally don't experience need recognition until they are exposed to advertising or see the product displayed on a store shelf. Consumers buy first and evaluate later, whereas the reverse is true for extensive decision making. A consumer who has previously purchased a whitening toothpaste and was satisfied with it will probably walk to the toothpaste aisle and select that same brand without spending 20 minutes examining all other alternatives.

Limited decision making typically occurs when a consumer has previous product experience but is unfamiliar with the current brands available. Limited decision making is also associated with lower levels of involvement (although higher than routine decisions) because consumers do expend moderate effort in searching for information or in considering various alternatives. But what happens if the consumer's usual brand of whitening toothpaste is sold out? If he or she needs toothpaste, the consumer will have to choose another brand. Before making a final decision, the consumer will likely evaluate several other brands based on their active ingredients, their promotional claims, and the consumer's prior experiences.

Consumers practice **extensive decision making** when buying an unfamiliar, expensive product or an infrequently bought item. This process is the most complex type of consumer buying decision and is associated with high involvement on the part of the consumer. This process resembles the model outlined in Exhibit 6.1. These consumers want to make the right decision, so they want to know as much as they can about the product category and available brands. People usually experience cognitive dissonance only when buying high-involvement products. Buyers use several criteria for evaluating their options and spend much time seeking information. Buying a home or a car, for example, requires extensive decision making.

Exhibit 6.2
Continuum of Consumer Buying Decisions

	Routine	Limited	Extensive
Involvement	low	low to moderate	high
Time	short	short to moderate	long
Cost	low	low to moderate	high
Information Search	internal only	mostly internal	internal and external
Number of Alternatives	one	few	many

The type of decision making that consumers use to purchase a product does not necessarily remain constant. For instance, if a routinely purchased product no longer satisfies, consumers may practice limited or extensive decision making to switch to another brand. And people who first use extensive decision making may then use limited or routine decision making for future purchases. For example, when a family gets a new puppy, they will spend a lot of time and energy trying out different toys to determine which one the dog prefers. Once the new owners learn that the dog prefers a bone to a ball, however, the purchase no longer requires extensive evaluation and will become routine.

FACTORS DETERMINING THE LEVEL OF CONSUMER INVOLVEMENT

The level of involvement in the purchase depends on the following five factors:

- *Previous experience:* When consumers have had previous experience with a good or service, the level of involvement typically decreases. After repeated product trials, consumers learn to make quick choices. Because consumers are familiar with the product and know whether it will satisfy their needs, they become less involved in the purchase. For example, a consumer purchasing cereal has many brands to choose from—just think of any grocery store cereal aisle. If the consumer always buys the same brand because it satisfies his hunger, then he has a low level of involvement. When a consumer purchases a cereal for the first time, however, it likely will be a much more involved purchase.
- *Interest:* Involvement is directly related to consumer interests, as in cars, music, movies, bicycling, or electronics. Naturally, these areas of interest vary from one individual to another. A person highly involved in bike racing will be very interested in the type of bike she owns and will spend quite a bit of time evaluating different bikes. If a person wants a bike only for recreation, however, he may be fairly uninvolved in the purchase and just choose a bike from the most convenient location.
- *Perceived risk of negative consequences:* As the perceived risk in purchasing a product increases, so does a consumer's level of involvement. The types of risks that concern consumers include financial risk, social risk, and psychological risk. First, financial risk is exposure to loss of wealth or purchasing power. Because high risk is associated with high-priced purchases, consumers tend to become extremely involved. Therefore, price and involvement are usually directly related: As price increases, so does the level of involvement. For example, someone who is purchasing a new car for the first time (higher perceived risk) will spend much more time and effort making this purchase than someone who has purchased several new cars (lower perceived risk). Second, consumers take social risks when they buy products that can affect people's social opinions of them (for example, driving an old, beat-up car or wearing unstylish clothes). Third, buyers undergo psychological risk if they feel that making the wrong decision might cause some concern or anxiety. For example, some consumers feel guilty about eating foods that are not healthy, such as regular ice cream rather than fat-free frozen yogurt.

© AP PHOTO/DAVID ZALUBOSKI

Car purchases are a high involvement task and today's buyers are looking closely at gas mileage.

- *Situation:* The circumstances of a purchase may temporarily transform a low-involvement decision into a high-involvement one. High involvement comes into play when the consumer perceives risk in a specific situation. For example, an individual might routinely buy low-priced brands of liquor and wine. When the boss visits, however, the consumer might make a high-involvement decision and buy more prestigious brands.
- *Social visibility:* Involvement also increases as the social visibility of a product increases. Products often

on social display include clothing (especially designer labels), jewelry, cars, and furniture. All these items make a statement about the purchaser and, therefore, carry a social risk.

MARKETING IMPLICATIONS OF INVOLVEMENT

Marketing strategy varies according to the level of involvement associated with the product. For high-involvement product purchases, marketing managers have several responsibilities. First, promotion to the target market should be extensive and informative. A good ad gives consumers the information they need for making the purchase decision, as well as specifying the benefits and unique advantages of owning the product. For example, a recent two-page ad for Toyota's Camry Hybrid provides extensive information on the personal and planet-wide benefits of driving the vehicle. Photos of a wide-eyed young girl and a globe are meant to appeal to the customer's care for the future, while captions on interior photos of the car and its engine note the vehicle's unique technology that "drives just like a regular car," benefits which might appeal to the consumer's need for performance.[7] Another ad featured in earlier pages of the same magazine shows the Camry Hybrid being driven along a country road, surrounded by green pastures and grazing horses. The ad targets the consumer who cares that the vehicle is built in the U.S. and that Toyota is committed to America, its air, its communities, and its future.[8]

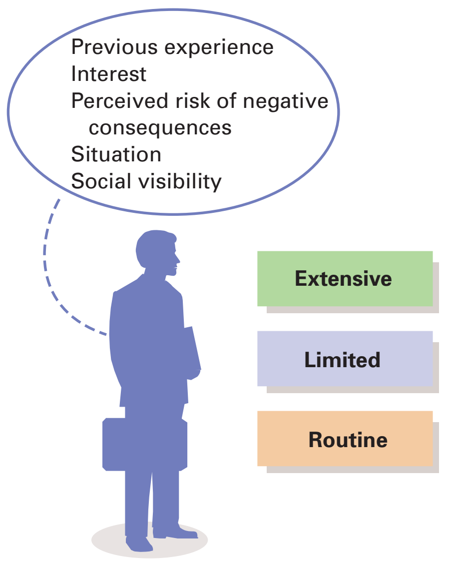
For low-involvement product purchases, consumers may not recognize their wants until they are in the store. Therefore, in-store promotion is an important tool when promoting low-involvement products. Marketing managers focus on package design so the product will be eye-catching and easily recognized on the shelf. Examples of products that take this approach are Campbell's soups, Tide detergent, Velveeta cheese, and Heinz ketchup. In-store displays also stimulate sales of low-involvement products. A good display can explain the product's purpose and prompt recognition of a want. Displays of health and beauty aid items in supermarkets have been known to increase sales many times above normal. Coupons, cents-off deals, and two-for-one offers also effectively promote low-involvement items.

Linking a product to a higher-involvement issue is another tactic that marketing managers can use to increase the sales or positive publicity of a low-involvement product. For example, in response to government and consumer concerns about childhood obesity, food manufacturers that advertise to children, such as Kellogg's, Hershey, McDonald's, and General Mills, have pledged to devote at least half of their marketing to the promotion of healthy dietary choices and lifestyles. In Kellogg's case, nearly $206 million in advertising dollars are at stake.[9]

REVIEW LEARNING OUTCOME

LO4

Identify the types of consumer buying decisions and discuss the significance of consumer involvement



Factors Influencing Consumer Buying Decisions

The consumer decision-making process does not occur in a vacuum. On the contrary, underlying cultural, social, individual, and psychological factors strongly influence the decision process. These factors have an effect from the time a consumer perceives a stimulus through postpurchase behavior.

Exhibit 6.3

Factors That Affect the Consumer Decision-Making Process

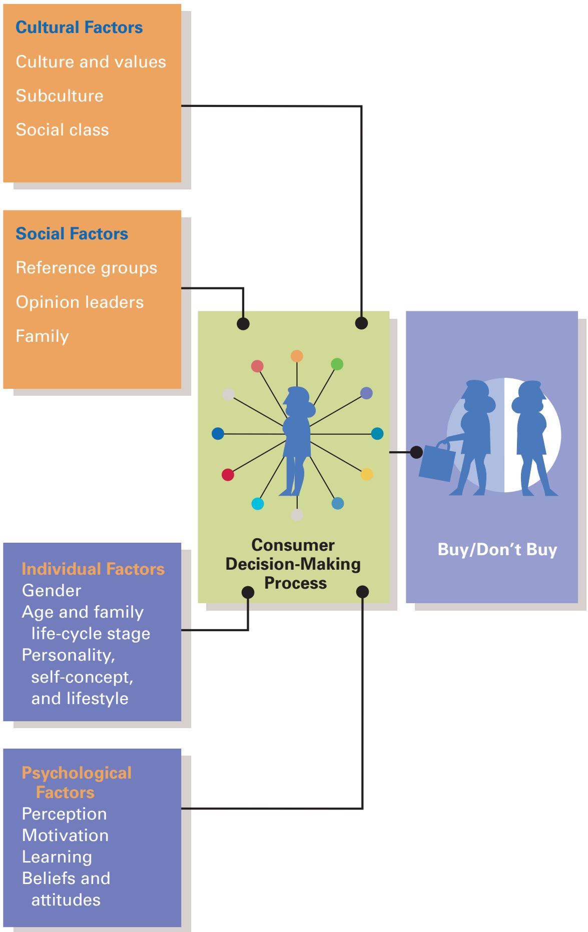


Exhibit 6.4

Components of American Culture

COMPONENT	EXAMPLES
Values	Success through hard work Emphasis on personal freedom
Language	English as the dominant language
Myths	George Washington never told a lie. Abraham Lincoln walked a mile to return a penny.
Customs	Bathing daily Shaking hands when greeting new people Standard gratuity of 15 to 20 percent at restaurants
Rituals	Thanksgiving Day dinner Singing the "Star Spangled Banner" before baseball games Going to religious services on the appropriate day
Laws	Child labor laws Sherman Anti-Trust Act guarantees competition
Material artifacts	Diamond engagement rings Cell phones

SOURCE: Adapted from *Consumer Behavior* by William D. Wells and David Prensky. Copyright (c) 1996 by John Wiley & Sons, Inc. Reprinted by permission of John Wiley & Sons, Inc. All Rights Reserved.

Cultural factors, which include culture and values, subculture, and social class, exert the broadest influence over consumer decision making. Social factors sum up the social interactions between a consumer and influential groups of people, such as reference groups, opinion leaders, and family members. Individual factors, which include gender, age, family life-cycle stage, personality, self-concept, and lifestyle, are unique to each individual and play a major role in the type of products and services consumers want. Psychological factors determine how consumers perceive and interact with their environments and influence the ultimate decisions consumers make. They include perception, motivation, learning, beliefs, and attitudes. Exhibit 6.3 summarizes these influences.

LO5

Cultural Influences on Consumer Buying Decisions

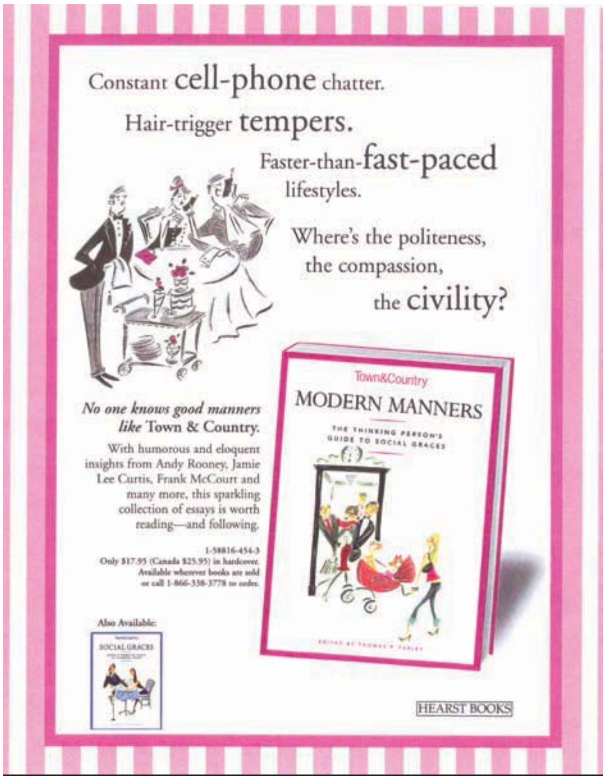
Of all the factors that affect consumer decision making, cultural factors exert the broadest and deepest influence. Marketers must understand the way people's culture and its accompanying values, as well as their subculture and social class, influence their buying behavior.

CULTURE AND VALUES

Culture is the essential character of a society that distinguishes it from other societal groups. The underlying elements of every culture are the values, language, myths, customs, rituals, and laws that shape the behavior of the people, as well as the material artifacts, or products, of that behavior as they are transmitted from one generation to the next. Exhibit 6.4 lists some defining components of American culture.

Culture is pervasive. Cultural values and influences are the ocean in which individuals swim, and yet most are completely unaware that it is there. What people eat, how they dress, what they think and feel, and what language they speak are all dimensions of culture. It encompasses all the things consumers do without conscious choice because their culture's values, customs, and rituals are ingrained in their daily habits.

Culture is functional. Human interaction creates values and prescribes acceptable behavior for each culture. By establishing common expectations, culture gives order to society. Sometimes these



Modern Manners explores the ways in which new technologies, such as cell-phones, have changed American culture.

expectations are enacted into laws. For example, drivers in our culture must stop at a red light. Other times these expectations are taken for granted. For example, grocery stores and hospitals are open 24 hours, whereas banks are open only during bankers' hours.

Culture is learned. Consumers are not born knowing the values and norms of their society. Instead, they must learn what is acceptable from family and friends. Children learn the values that will govern their behavior from parents, teachers, and peers. As members of our society, they learn to shake hands when they greet someone, to drive on the right-hand side of the road, and to eat pizza and drink Coca-Cola.

Culture is dynamic. It adapts to changing needs and an evolving environment. The rapid growth of technology in today's world has accelerated the rate of cultural change. Television has changed entertainment patterns and family communication and has heightened public awareness of political and other news events. Automation has increased the amount of leisure time we have and, in some ways, has changed the traditional work ethic. Cultural norms will continue to evolve because of our need for social patterns that solve problems.

In the United States, rapidly increasing diversity is causing major shifts in culture. For example, the growing Hispanic community influences American food, music, clothing, and entertainment. Additionally, African American culture has been embraced by the mainstream. Indeed, African American women make up one of the fastest-growing segments of the American population. The projected growth rate of this segment is 8 percent, compared to 4 percent for the total U.S. population. Additionally, one in two married black women is the primary decision maker in buying a house, versus one in four married white women. Traditionally, marketers have not taken advantage of the opportunity to market to African American women. Now, however, many companies are taking note of this rapidly growing segment of the population. For example, Kraft's Honey Bunches of Oats cereal developed an advertising campaign especially for black women. Research suggested that African American women do not like to eat cereal when others are present, so the print ad shows a black woman eating a bowl of cereal alone with the caption "Take a breather. This moment is yours. Just you and your bowl of Honey Bunches of Oats."[10]

The most defining element of a culture is its values—the enduring beliefs shared by a society that a specific mode of conduct is personally or socially preferable to another mode of conduct. People's value systems have a great effect on their consumer behavior. Consumers with similar value systems tend to react alike to prices and other marketing-related inducements. Values also correspond to consumption patterns. For example, Americans place a high value on convenience. This value has created lucrative markets for products such as breakfast bars, energy bars, and nutrition bars that allow consumers to eat on the go. Values can also influence consumers' TV viewing habits or the magazines they read. For instance, people who strongly object to violence avoid crime shows, and those who oppose pornography do not buy *Hustler*. Core American values—those considered central to the American way of life—are presented in Exhibit 6.5.

The personal values of target consumers have important implications for marketing managers. When marketers understand the core values that underlie the attitudes that shape the buying patterns of America's consumers and how these values were molded by experiences, they can target their message more effectively. For example, the personal value systems of older consumers, baby boomers,

culture
The set of values, norms, attitudes, and other meaningful symbols that shape human behavior, and the artifacts, or products, of that behavior as they are transmitted from one generation to the next.

value
The enduring belief that a specific mode of conduct is personally or socially preferable to another mode of conduct.

Exhibit 6.5

Core American Values

Success	Americans admire hard work, entrepreneurship, achievement, and success. Those achieving success in American society are rewarded with money, status, and prestige. For example, Bill Gates, once a nerdy computer buff, built Microsoft Corporation into an internationally known giant. Gates is now one of the richest people in the world.
Materialism	Americans value owning tangible goods. American society encourages consumption, ownership, and possession. Americans judge others based on their material possessions; for example, the type of car they own, where they live, and what type of clothes they wear.
Freedom	The American culture was founded on the principle of religious and political freedom. The U.S. Constitution and the Bill of Rights assure American citizens the right to life, liberty, and the pursuit of happiness. These freedoms are fundamental to the legal system and the moral fiber of American culture. The Internet, for example, is built on the principle of the right to free speech. Lawmakers who have attempted to limit the material available on the Internet have met with tough opposition from proponents of free speech. Spam has become such a major problem in recent years, however, that individuals are becoming more receptive to laws restricting spam even if they limit spammers' free speech.
Progress	Technological advances, as well as advances in medicine, science, health, and the quality of products and services, are important to Americans. Each year, for example, more than 20,000 new or improved consumer products are introduced on America's supermarket shelves.*
Youth	Americans are obsessed with youth and spend a good deal of time on products and procedures that make them feel and look younger. Americans spend millions each year on health and beauty aids, health clubs, and healthy foods. Media and advertising encourage the quest for youth by using young, attractive, slim models, such as those in ads from fashion designer Calvin Klein.
Capitalism	Americans believe in a free enterprise system characterized by competition and the chance for monetary success. Capitalism creates choices, quality, and value for Americans. Laws prohibit monopolistic control of a market and regulate free trade. Americans encourage small business success, such as that found by Apple Computer, Wal-Mart, and McDonald's, all of which started as small enterprises with a better idea that toppled the competition.

*Data obtained from the Food Marketing Institute Web site at **http://www.fmi.org,** 2004.
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Generation Xers, and Generation Yers are quite different. The key to understanding older consumers, or everyone born before 1945, is recognizing the impact of the Great Depression and World War II on their lives. Facing these two immense challenges shaped a generation characterized by discipline, self-denial, financial and social conservatism, and a sense of obligation. Boomers, those individuals nurtured in the bountiful postwar period between 1946 and 1964, believe they are entitled to the wealth and opportunity that seemed endless in their youth, although they are proud of their strong work ethic. Self-improvement is a major motivator of the boomer generation. Generation Xers, born between 1965 and 1978, are very self-reliant and accepting of diversity and individuality. They are also a very entrepreneurial-driven generation, ready to tackle life's challenges for themselves rather than as part of a crowd.[11] Gen Yers, born between 1979 and 1994, are more serious and socially conscious than Gen Xers. Some of the defining events of their lives include Columbine, the O. J. Simpson trial, the Clinton impeachment, the 2000 presidential election, and the terrorist attacks of September 11, 2001. They grew up with cable television, computers, debit cards, and cell phones, making them the most well-connected generation to date—a fact that has important implications for word-of-mouth influence.[12]

Values represent what is most important in people's lives. Therefore, marketers watch carefully for shifts in consumers' values over time. For example, millions of Americans have an interest in spirituality, as evidenced by the soaring sales of books with religious or spiritual themes and the popularity of television shows with similar themes. Similarly, after the September 11 terrorist attacks, when many people were fearful and concerned about self-protection, gun sales increased dramatically as did the sale of drugs to cure anthrax.

James Stengel, global marketing director for Procter & Gamble, had this to say about the changes he's seen in today's consumers, "The biggest thing going on with U.S. consumers is that they want to trust something. They want to be understood, they want to be respected, [and] they want to be listened to. They don't want to be talked to. It's trust in the largest sense of the word. People really do care what's behind the brand, what's behind the business. They care about the values of a brand and the values of a company. We can never forget that. We can never be complacent about that."[13]

UNDERSTANDING CULTURAL DIFFERENCES

As more companies expand their operations globally, the need to understand the cultures of foreign countries becomes more important. A firm has little chance of selling products in a culture it does not understand. Like people, products have cultural values and rules that influence their perception and use. Culture, therefore, must be understood before the behavior of individuals within the cultural context can be understood. Colors, for example, may have different meanings in global markets than they do at home. In China, white is the color of mourning, and brides wear red. In the United States, black represents mourning, and brides wear white.

Language is another important aspect of culture that global marketers must deal with. When translating product names, slogans, and promotional messages into foreign languages, marketers should take care to avoid conveying the wrong message. General Motors discovered too late that Nova (the name of an economical car) literally means "doesn't go" in Spanish; Coors encouraged its English-speaking customers to "Turn it loose," but the phrase in Spanish means "Suffer from diarrhea."

Though marketers expanding into global markets generally adapt their products and business formats to the local culture, some fear that increasing globalization, along with the proliferation of the Internet, will ultimately result in a homogeneous world culture in the future. U.S. companies in particular, they fear, are Americanizing the world by exporting bastions of American culture, such as McDonald's fast-food restaurants, Starbucks coffeehouses, Microsoft software, and American movies and entertainment.

SUBCULTURE

subculture
A homogeneous group of people who share elements of the overall culture as well as unique elements of their own group.

A culture can be divided into subcultures on the basis of demographic characteristics, geographic regions, national and ethnic background, political beliefs, and religious beliefs. A subculture is a homogeneous group of people who share elements of the overall culture as well as cultural elements unique to their own group. Within subcultures, people's attitudes, values, and purchase decisions are even more similar than they are within the broader culture. Subcultural differences may foster considerable variation within a culture in terms of which, how, when, and where people buy goods and services.

In the United States alone, countless subcultures can be identified. Many are concentrated geographically. People belonging to the Mormon religion, for example, are clustered mainly in Utah; Cajuns are located in the bayou regions of southern Louisiana. Many Hispanics live in states bordering Mexico, whereas the majority of Chinese, Japanese, and Korean Americans are found on the West Coast. Other subcultures are geographically dispersed. Computer hackers, people who are hearing or visually impaired, Harley-Davidson bikers, military families, university professors, and gays may be found throughout the country. Yet they have identifiable attitudes, values, and needs that distinguish them from the larger culture.

Once marketers identify subcultures, they can design special marketing programs to serve their needs. According to the U.S. Census Bureau, the Hispanic population is the largest and fastest-growing subculture, increasing four times as fast as the general population. To tap into this large and growing segment, marketers have been forming partnerships with broadcasters that have established Latino audiences. For example, State Farm Insurance partnered with Univision Radio, a Spanish-language formatted station, to sponsor the 2006 World Cup soccer games. The Univision Radio network covers approximately 73 percent of the U.S. Hispanic

Exhibit 6.6

U.S. Social Classes

Upper Classes		
Capitalist class	1 percent	People whose investment decisions shape the national economy; income mostly from assets, earned or inherited; university connections
Upper middle class	14 percent	Upper-level managers, professionals, owners of medium-sized businesses; well-to-do, stay-at-home homemakers who decline occupational work by choice; college-educated; family income well above national average
Middle Classes		
Middle class	33 percent	Middle-level white-collar, top-level blue-collar; education past high school typical; income somewhat above national average; loss of manufacturing jobs has reduced the population of this class
Working class	32 percent	Middle-level blue-collar, lower-level white-collar; income below national average; largely working in skilled or semi-skilled service jobs
Lower Classes		
Working poor	11–12 percent	Low-paid service workers and operatives; some high school education; below mainstream in living standard; crime and hunger are daily threats
Underclass	8–9 percent	People who are not regularly employed and who depend primarily on the welfare system for sustenance; little schooling; living standard below poverty line

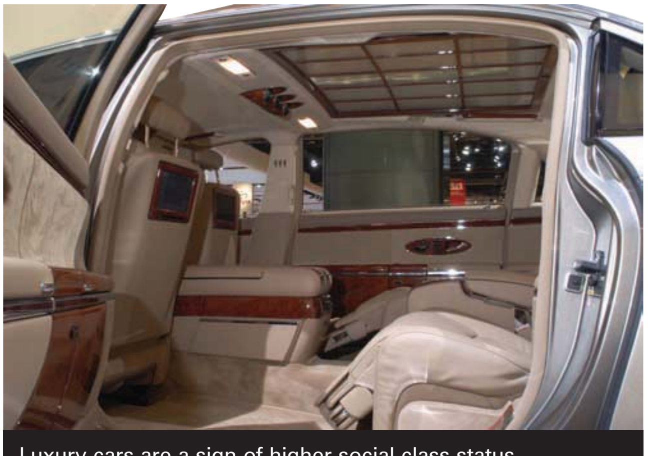
SOURCE: Adapted from Richard P. Coleman, "The Continuing Significance of Social Class to Marketing," Journal of Consumer Research, December 1983, 267; Dennis Gilbert and Joseph A. Kahl, The American Class Structure: A Synthesis (Homewood, IL: Dorsey Press, 1982), ch. 11, accessed online at **http://en.wikipedia.org/wiki/social_structure_of_the_united_states,** May 2008.

social class
A group of people in a society who are considered nearly equal in status or community esteem, who regularly socialize among themselves both formally and informally, and who share behavioral norms.

population and has over 10 million listeners weekly. State Farm also partnered with Julie Stav, the leading financial expert for the Latino community, to sponsor evening broadcasts of her hugely successful Spanish-language radio show.[14] When Sweden-based furniture manufacturer IKEA realized it wasn't capturing the large Latino demographic in U.S. cities, it started advertising in Spanish. It also launched a series of commercials featuring Latina soap opera stars on Telemundo—the second-largest U.S. Spanish-language broadcaster. IKEA saw an immediate increase in the number of Latinos visiting its stores.[15]

SOCIAL CLASS

The United States, like other societies, has a social class system. A social class is a group of people who are considered nearly equal in status or community esteem, who regularly socialize among themselves both formally and informally, and who share behavioral norms.



© MARK SCHEUERN/ALAMY

Luxury cars are a sign of higher social class status.

A number of techniques have been used to measure social class, and a number of criteria have been used to define it. One view of contemporary U.S. status structure is shown in Exhibit 6.6.

As you can see from Exhibit 6.6, the upper and upper middle classes comprise the small segment of affluent and wealthy Americans. The upper social classes are more likely than other classes to contribute something to society—for example, by volunteer work or active participation in civic affairs. In terms of consumer buying patterns, the affluent are more likely to own their own home and purchase new cars and trucks and are less likely to smoke. The very rich flex their financial muscles by spending more on vacation homes, vacations and cruises, and housekeeping and gardening services. The most affluent consumers are more likely to attend art auctions and galleries, dance performances, operas, the theater, museums, concerts, and sporting events. Marketers often pay attention to the superwealthy. For example, the Mercedes-Benz Maybach 62, touted as the "world's most luxurious car," is aimed at this group. Priced at $375,000, the car features electronic doors, reclining seats with footrests, a workstation with media capability, a champagne cooler, and other luxuries. Similarly, New York-based designer Calvin Stewart sells A.P.O. jeans featuring fully customized denim embellished with diamond, gold, and platinum details—starting at $1,000 a pair.[16]

The majority of Americans today define themselves as middle class, regardless of their actual income or educational attainment. This phenomenon most likely occurs because working-class Americans tend to aspire to the middle-class lifestyle while some of those who do achieve affluence may downwardly aspire to respectable middle-class status as a matter of principle. Attaining goals and achieving status and prestige are important to middle-class consumers. People falling into the middle class live in the gap between the haves and the have-nots. They aspire to the lifestyle of the more affluent, but are constrained by the economic realities and cautious attitudes they share with the working class.

The working class is a distinct subset of the middle class. Interest in organized labor is one of the most common attributes among the working class. This group often rates job security as the most important reason for taking a job. The working-class person depends heavily on relatives and the community for economic and emotional support. This emphasis on family ties is one sign of the group's intensely local view of the world. They seek local news far more often than middle-class audiences, which favor national and world coverage. They also tend to vacation closer to home.

Lifestyle distinctions between the social classes are greater than the distinctions within a given class. The most significant difference between the classes occurs between the middle and lower classes, where there is a major shift in lifestyles. Members of the lower class typically have incomes at or below the poverty level. This social class has the highest unemployment rate, and many individuals or families are subsidized through the welfare system. Many are illiterate, with little formal education. Compared to more affluent consumers, lower-class consumers have poorer diets and typically purchase very different kinds of foods when they shop.

Social class is typically measured as a combination of occupation, income, education, wealth, and other variables. For instance, affluent upper-class consumers are more likely to be salaried executives or self-employed professionals with at least an undergraduate degree. Working-class or middle-class consumers are more likely to be hourly service workers or blue-collar employees with only a high school education. Educational attainment, however, seems to be the most reliable indicator of a person's social and economic status (see Exhibit 6.7). Those with college degrees or graduate degrees are more likely to fall into the upper classes, while those people with some college experience fall closest to traditional concepts of the middle class.

Marketers are interested in social class for two main reasons. First, social class often indicates which medium to use for advertising. Suppose an insurance company hopes to sell its policies to middle-class families. It might advertise during the local evening news because middle-class families tend to watch more television than other classes do. If the company wants to sell more policies to upscale individuals, it might place a print ad in a business publication like *The Wall Street Journal*. The Internet, long the domain of more educated and affluent families, is becoming an increasingly important advertising outlet for advertisers hoping to

Exhibit 6.7

Social Class and Education

Educational Profile	Median Household Income
Those with less than a 9th grade education	$ 17,261
Those with a 9th–12th grade education (no diploma)	$ 21,737
High school graduates	$ 35,744
College graduates, B.A.	$ 64,406
College graduates, M.A.	$ 74,476
Professional degree holders	$ 100,000

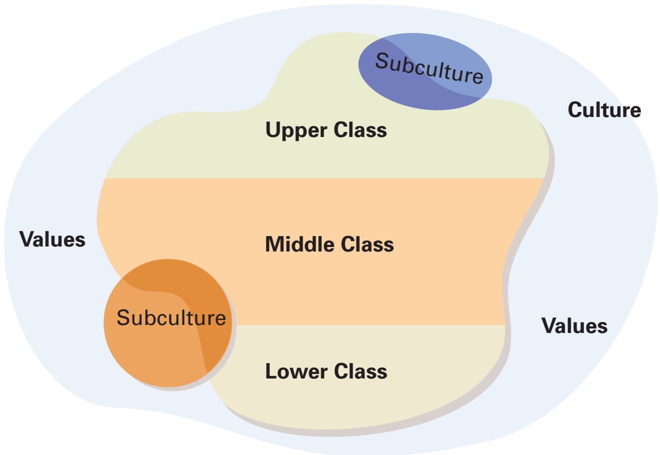
SOURCE: U.S. Census Bureau, 1999, accessed online at **http://www.pbs.org/peoplelikeus/resources/stats.html,** May 2006 reach blue-collar workers and homemakers. As the middle class rapidly adopts the medium, marketers must research which Web sites will reach their audience.

Second, knowing what products appeal to which social classes can help marketers determine where to best distribute their products. Affluent Americans, a fifth of the U.S. population, are responsible for nearly half of all new car and truck sales and over half of hotel stays and vacation homes. This same group spends nearly twice as much as less-affluent Americans on restaurant fare, alcohol, sporting events, plays, and club memberships.[17]

For the first time in a long while, however, industry analysts note that shares of discount chains are faring better than their full-priced and upscale counterparts. These days, analysts say, the big-box and discount retailers' greatest challenge is courting consumers who fall in the middle-income level. The result is a fiercely competitive retail environment in which discount retailers focus less on their core, low-income consumers, who are most effected by rising housing and gas costs. Given the current penny-pinching economy however, shares of discount chains are faring better than those of their full-priced and upscale counterparts, because discount retailers focus on getting current customers to purchase a wider array of products in the store, instead of struggling to attract new shoppers.[18]

REVIEW LEARNING OUTCOME

LO5 Identify and understand the cultural factors that affect consumer buying decisions



LO6 Social Influences on Consumer Buying Decisions

Most consumers are likely to seek out the opinions of others to reduce their search and evaluation effort or uncertainty, especially as the perceived risk of the decision increases. Consumers may also seek out others' opinions for guidance on new products or services, products with image-related attributes, or products for which attribute information is scarce or unhelpful. Consumers interact socially with reference groups, opinion leaders, and family members to obtain product information and decision approval.

REFERENCE GROUPS

reference group
A group in society that influences an individual's purchasing behavior.

All the formal and informal groups that influence the buying behavior of an individual are that person's **reference groups**. Consumers may use products or brands to identify with or become a member of a group. They learn by observing how members of their reference groups consume, and they use the same criteria to make their own consumer decisions.

Reference groups can be categorized very broadly as either direct or indirect (see Exhibit 6.8). Direct reference groups are face-to-face membership groups that touch people's lives directly. They can be either primary or secondary.

Primary membership groups include all groups with which people interact regularly in an informal, face-to-face manner, such as family, friends, and coworkers. In contrast, people associate with secondary membership groups less consistently and more formally. These groups might include clubs, professional groups, and religious groups.

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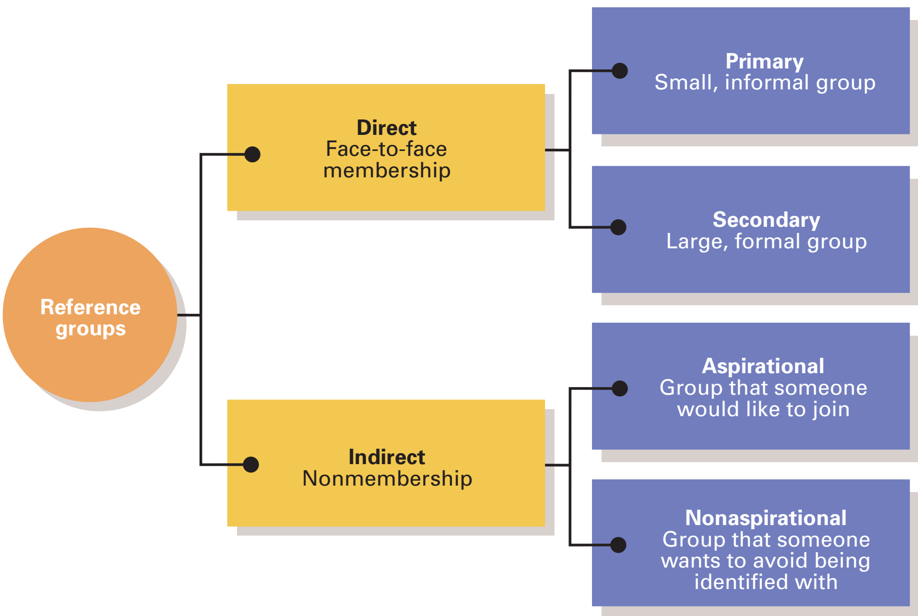
Consumers also are influenced by many indirect, nonmembership reference groups they do not belong to. Aspirational reference groups are those a person would like to join. To join an aspirational group, a person must at least conform to the norms of that group. (Norms are the values and attitudes deemed acceptable by the group.) Thus, a person who wants to be elected to public office may begin to dress more conservatively, as other politicians do. He or she may go to many of the restaurants and social engagements that city and business leaders attend and try to play a role that is acceptable to voters and other influential people. Similarly, teenagers may dye their hair and experiment with body piercing and tattoos. Athletes are an aspirational group for several market segments. To appeal to the younger market, Coca-Cola signed basketball star LeBron James to be the spokesperson for its Sprite and POWERade brands, and Nike signed a sneaker deal, reportedly worth $90 million, with him. Coca-Cola and Nike assumed James would encourage consumers to drink Coke brands and buy Nike shoes in order to identify with him. As his popularity grows, so do his contracts. LeBron recently signed endorsement deals with PepsiCo's Gatorade, Lincoln-Mercury, and T-Mobile.[19] Read the "Global Perspectives" box for an example of how aspirational brands and social class have created a unique market in China.

Nonaspirational reference groups, or dissociative groups, influence our behavior when we try to maintain distance from them. A consumer may avoid buying some types of clothing or cars, going to certain restaurants or stores, or even buying a home in a certain neighborhood in order to avoid being associated with a particular group.

Exhibit 6.8
Types of Reference Groups



The activities, values, and goals of reference groups directly influence consumer behavior. For marketers, reference groups have three important implications: (1) they serve as information sources and influence perceptions; (2) they affect an individual's aspiration levels; and (3) their norms either constrain or stimulate consumer behavior. For example, research firms devoted to uncovering what's cool in the teen market, have identified a couple of influential groups among today's

primary membership group
A reference group with which people interact regularly in an informal, face-to-face manner, such as family, friends, or fellow employees.

secondary membership group
A reference group with which people associate less consistently and more formally than a primary membership group, such as a club, professional group, or religious group.

aspirational reference group
A group that someone would like to join.

norm
A value or attitude deemed acceptable by a group.

nonaspirational reference group
A group with which an individual does not want to associate.

teens based on their interests in clothes, music, and activities. Tracking these groups reveals how products become cool and how groups influence the adoption of cool products by other groups. A trend or fad often starts with teens who have the most innovative tastes. These teens are on the cutting edge of fashion and music, and they wear their attitude all over their bodies in the form of tattoos, body piercing, studded jewelry, or colored tresses. Certain fads embraced by these "Edgers" will spark an interest in the small group of teens researchers call "Influencers," who project the look other teens covet. Influencers also create their own trends in music and clothing choices. Once a fad is embraced and adopted by Influencers, the look becomes cool and desirable. The remaining groups comprising the majority of the teen population will not embrace a fad until it gets its seal of approval from the Influencers.

Understanding the effect of reference groups on a product is important for marketers as they track the life cycle of their products. Retailer Abercrombie & Fitch noticed it was losing its target audience of college students as its stores began attracting large numbers of high school students trying to emulate college students. To solve the problem, A&F created its Hollister store chain specifically for high school students. The retailer also opened a chain called Abercrombie for a target market of boys and girls, ages seven to fourteen. Another A&F chain, Ruehl, offers Greenwich Village-inspired clothing for the post-college-age market.[20]

Marketers and researchers can gauge teen opinions, test new product ideas, and even get help creating marketing buzz by tapping into ever-expanding online teen communities. For example, Piczo, an online community with 28 million registered users worldwide, has a group of influential "insiders" who will advise brands on how to best leverage the site. Essentially a focus group, "Piczo Insiders" exchange opinions and offer feedback on marketing campaigns running on the Piczo site. These teens collaborate online with marketers and respond to any research activity or project that they think will improve the Piczo user experience. The Insiders recently contributed real-life stories to "Don't Hide It," a successful new campaign for the National Society for the Prevention of Cruelty to Children (NSPCC).[21]

GLOBAL Perspectives

The Chinese Consumer

With over 1.3 billion potential consumers, China is the world's largest consumer market, and its people grow richer and more status-conscious every year. Marketers can easily appreciate the opportunities offered by such a vast market, but more challenging is understanding that market's buying behavior. Who exactly are Chinese consumers? How much money do they have? What do they want to purchase? What motivates them to buy?

There is no single answer. China has a variety of consumer cultures and economic systems. Even though much of the population is rural and poor, a strong middle class is emerging, and China counts approximately 25 million middle-class households and about 8 million affluent households. Less than one half of 1 percent of the population holds 60 percent of the nation's wealth.

Booming economies, like the one that has propelled China for the past decade, tend to drive consumer behavior in new ways. In particular, aspirational buying behaviors among the growing middle-class have increased. Traditionally, the Chinese consumer has been a saver rather than a spender and has viewed wealth as security—protection against future adversities. But today's economic growth has changed the way the Chinese look at brands and at themselves as consumers. Many Chinese have come to see money as a kind of freedom, one that includes the opportunity to be wooed by brands. Armani, Rolex, BMW, Louis Vuitton, and DeBeers are favorite luxury brands in China, and in recent years, Bentley has sold more cars in China than in any other country. Complex cultural differences, though, make some brands unusually popular, compared to their stature in the U.S., for instance. Procter & Gamble's Olay is an "aspirational brand" in China because it is not only selling its message to "love your skin," as it does in the U.S., but also says "Olay will get you a rich husband."

What do you think makes China such a complex challenge for marketers? What opportunities can you envision for global marketers in China? For domestic marketers?

SOURCE: Sheridan Prasso, "China's New Cultural Revolution," *Fortune,* May 17, 2007; "One Billion, Three Hundred Million: The New Chinese Consumer," Knowledge @Wharton, October 16, 2007.

OPINION LEADERS

opinion leader
An individual who influences the opinions of others.

Reference groups frequently include individuals known as group leaders, or opinion leaders—those who influence others. Obviously, it is important for marketing managers to persuade such people to purchase their goods or services. Many products and services that are integral parts of Americans' lives today got their initial boost from opinion leaders. For example, DVDs and SUVs (sport-utility vehicles) were purchased by opinion leaders well ahead of the general public.

Opinion leaders are often the first to try new products and services out of pure curiosity. They are typically self-indulgent, making them more likely to explore unproven but intriguing products and services. Technology companies know that teenagers, because of their willingness to experiment, are key opinion leaders for the success of new technologies.

Opinion leadership is a casual, face-to-face phenomenon and is usually inconspicuous, so locating opinion leaders can be a challenge. Thus, marketers often try to create opinion leaders. They may use high school cheerleaders to model new fall fashions or civic leaders to promote insurance, new cars, and other merchandise. On a national level, companies sometimes use movie stars, sports figures, and other celebrities to promote products, hoping they are appropriate opinion leaders. The effectiveness of celebrity endorsements varies, though, depending largely on how credible and attractive the spokesperson is and how familiar people are with him or her. Endorsements are most likely to succeed if marketers can establish a reasonable association between the spokesperson and the product.

Celebrities and sports figures aren't the only people marketers consider opinion leaders, however. Managers at BMW are rethinking who the ideal U.S. opinion leaders for their brand. Historically, the automaker targeted car enthusiasts. Today, the company is looking at the "idea class," a group comprised of roughly 1.5 million architects, professionals, innovators, and entrepreneurs who are more interested in design, authenticity, and independent thinking. Over a five-year period, BMW has increased U.S. sales by 62 percent, but still has less than a 2 percent share of the U.S. market.[22]

Respected organizations, such as the American Heart Association and the American Cancer Society, may also serve as opinion leaders. Marketers may seek endorsements from them as well as from schools, churches, cities, the military, and fraternal organizations as a form of group opinion leadership. Salespeople often ask to use opinion leaders' names in order to achieve greater personal influence in a sales presentation.

How Blogs Are Defining Today's Opinion Leaders

Increasingly, marketers are looking to Web logs, or blogs, as they're commonly called, to find opinion leaders.[23] According to Technorati, a blog-monitoring site, one new blog is created every second of every day, so it's getting harder to separate the true opinion leaders from intermediate Web users who simply want to share random thoughts or vacation photos with family and friends. As of this printing, Technorati monitors 35.3 million blogs, Feedster monitors 80 million, and Nielsen BuzzMetrics boasts coverage of more than 25 million blogs.[24] The fashion industry once dismissed bloggers as irrelevant and small-time, and limited their access to hot events during semi-annual fashion week shows. Now, however, fashion bloggers have the attention of the fashion establishment because many claim bigger followings than traditional media. Still, not all fashion blogs are equal. Bloggers from FashionTribes.com and Bagtrends.com received tickets to some fall 2006 shows, but shopology.com and Coutorture.com were denied access because their audiences were too small.[25]

One way marketers are identifying true opinion leaders is by looking to teen blogs to identify the current social trends shaping consumer behavior. During the research phase of development for its teen-targeted RED Blogs service, AOL

Exhibit 6.9

Tweens and Teens Weigh In On Advertising Tactics

Ad Tactic	Like		Dislike	
	8-12 yrs	13-18 yrs	8-12 yrs	13-18 yrs
Famous person uses product	39%	21%	12%	22%
Person in a movie uses product	33%	20%	12%	19%
Cartoon or TV show about product	31%	13%	25%	34%
Popular kids given free product	24%	12%	43%	44%
Product advertised on cell phones	5%	4%	41%	55%
Product mentioned in online chats	5%	4%	37%	45%
Product written about on a blog site	14%	10%	24%	32%

SOURCE: Based on "Today's Youth Look to Advertising as Much as Their Friends When Making Purchase Decisions", 'PR Newswire', August 21, 2006.

discovered that over 50 percent of teens do not mind sharing their feelings in public forums. This is especially evident at social networking sites like Myspace, FaceBook, and Xanga, where teens and twenty-somethings post extensive personal profiles, photo collections, links to user groups they belong to, and detailed descriptions of their social events.

Raised with MTV, 500-channel cable services, a rapidly maturing Internet, and ever-expanding cell phone capabilities, teens have unprecedented access to the world around them. Furthermore, they are no longer passive observers of the culture their parents created. They can follow their favorite bands, actors, or athletes via their Web sites and blogs and expect to interact with them instead of just admiring them from afar. With their unprecedented ability to network and communicate with one another, young people rely on each others' opinions more than marketing messages when making purchase decisions. And blogs are becoming a key way that teens communicate their opinions. Consequently, today's marketers are reading teen blogs, developing products that meet the very specific needs that teens express there, and are learning unique and creative ways to put key influencers in charge of marketing their brands for them.

FAMILY

socialization process
How cultural values and norms are passed down to children.

The family is the most important social institution for many consumers, strongly influencing values, attitudes, self-concept—and buying behavior. For example, a family that strongly values good health will have a grocery list distinctly different from that of a family that views every dinner as a gourmet event. Moreover, the family is responsible for the **socialization process**, the passing down of cultural values and norms to children. Children learn by observing their parents' consumption patterns, and so they will tend to shop in a similar pattern.

Decision-making roles among family members tend to vary significantly, depending on the type of item purchased. Family members assume a variety of roles in the purchase process. *Initiators* suggest, initiate, or plant the seed for the purchase process. The initiator can be any member of the family. For example, Sister might initiate the product search by asking for a new bicycle as a birthday present. *Influencers* are those members of the family whose opinions are valued. In our example, Mom might function as a price-range watchdog, an influencer whose main role is to veto or approve price ranges. Brother may give his opinion on certain makes of bicycles. The *decision maker* is the family member who actually makes the decision to buy or not to buy. For example, Dad or Mom is likely to choose the final brand and model of bicycle to buy after seeking further information from Sister about cosmetic features such as color, and then imposing additional criteria of his or her own, such as durability and safety. The *purchaser* (probably Dad or Mom) is the one who actually exchanges money for the product. Finally, the *consumer* is the actual user—Sister, in the case of the bicycle.

Marketers should consider family purchase situations along with the distribution of consumer and decision-maker roles among family members. Ordinary marketing views the individual as both decision maker and consumer. Family marketing adds several other possibilities: Sometimes more than one family member or all family members are involved in the decision; Sometimes only children are involved in the decision; Sometimes more than one consumer

Exhibit 6.10

Relationships among Purchasers and Consumers in the Family

Consumer	Purchase Decision Maker: Parent(s) Only	Purchase Decision Maker: Child/Children Only	Purchase Decision Maker: Some or All Family Members
Parent(s)	golf clubs cosmetics wine	Mother's Day card	Christmas gifts minivan
Child/Children	diapers breakfast cereal	candy small toys	bicycle
Some Family Members	videos long-distance phone service	children's movies	computers sports events
All Family Members	clothing life insurance	fast-food restaurant	swim club membership vacations

SOURCE: Reprinted with permission from "Pulling the Family's Strings" by Robert Boutillier in the August issue of 'American Demographics.'

REVIEW LEARNING OUTCOME

LO6 Identify and understand the social factors that affect consumer buying decisions

Reference Groups	Direct		Indirect	
	Primary	Secondary	Aspirational	Nonaspirational

Opinion Leaders	People you know	Celebrities

Family	Socialization Process
	Initiators, Influencers, Decision Makers, Purchasers, Consumers

is involved; Sometimes the decision maker and the consumer are different people. Exhibit 6.10 represents the possible patterns of family purchasing relationships.

Children can have great influence over the purchase decisions of their parents. In many families, with both parents working and short on time, children are encouraged to participate. In addition, children in single-parent households become more involved in family decisions at an earlier age. Children are especially influential in decisions about food and eating out. Exactly how much of an influence kids have varies depending on such factors as age, race, socioeconomic status, and region. For example, Restaurants & Institutions' New American Diner study shows that children age 5 or younger frequently influence restaurant visits, while children ages 6 to 18 have only occasional influence. Females, Generation Xers, Asian Americans, and Midwesterners are most likely to say children influence which restaurants they visit.[26] Children influence purchase decisions for many more products and services than food. Even though they are usually not the actual purchasers of such items, children often participate in decisions about toys, clothes, vacations, recreation, automobiles, and many other products. And if those children happen to be teenagers? American teens have a total income of $80 billion of their own, and parents spend an additional $110 billion each year on them. Recent data shows that while teens make up only 7 percent of the U.S. population, they actually contribute to 11 percent of U.S. spending.[27]

LO7

Individual Influences on Consumer Buying Decisions

A person's buying decisions are also influenced by personal characteristics that are unique to each individual, such as gender; age and life-cycle stage; and personality, self-concept, and lifestyle. Individual characteristics are generally stable over the course of one's life. For instance, most people do not change their gender, and the act of changing personality or lifestyle requires a complete reorientation of one's life. In the case of age and life-cycle stage, these changes occur gradually over time.

GENDER

Physiological differences between men and women result in different needs, such as health and beauty products. Just as important are the distinct cultural, social, and economic roles played by men and women and the effects that these have on their decision-making processes. For example, many networks have programming targeted to women, while Spike TV calls itself the "first network for men." Two magazines are geared to men who like to shop: *Details* is an upscale fashion magazine for affluent men in their 20s and 30s; *Complex* is a magazine for younger men whose fashions range from hip-hop and skateboarding to mainstream style.[28]

Trends in gender marketing are influenced by the changing roles of men and women in society. For example, men used to rely on the women in their lives to shop for them. Today, however, more men are shopping for themselves. The number of men shopping online was up to 57 percent in 2007 from 38 percent in 2006. Census Bureau figures show that in March, 2003, the latest year for which Census statistics are available, there were 299,000 married-family households in which the husband was at home with at least one child under six. This figure was up 29 percent from 1993.[29] Men who stay at home with their young children have begun to notice how few baby items, like diaper bags, are made with men's use in mind. One man even created his own product line, at **dadgear.com**. The first year the products hit the market, revenue was slightly higher than $40,000; projected revenue for 2006 was $800,000 to $1 million.[30] Whether because of the advent of online shopping or retailers wising up to the way men like to shop, today more men are comfortable shopping for themselves. A study commissioned by GQ found that 84 percent of men said they purchase their own clothes, compared with 65 percent four years ago.[31]

Men's roles aren't the only ones that are changing. Women around the world are working and earning more, and many industries are attracting new customers by marketing to women. For example, nearly 40 percent, or 50 million, of American Airlines' customers are women. If AA raises that number by 2 percent, it will make another $94 million in revenue each year. Therefore, American has launched an online community resource especially for women travelers at **www.aa.com/women**.[32] Wyndham Hotels and Resorts developed a program called Women On Their Way® to enhance the experience of their female guests. [33] American and Wyndham believe that by listening and responding to their female customers' insights, they can improve the travel experience for all of their. These special programs are also designed to foster women travelers' belief that their business is valued.

The changing roles of women are also forcing companies that have traditionally targeted women to develop new strategies. This is partly women's decision making tends to be multi-minded and integrative; they consider many criteria and move back and forth among them instead of focusing single-mindedly on a single feature. They tend to view shopping as a learning process. They educate themselves about the available options and typically add criteria as they learn more. It is not unusual for a woman to shift back to an earlier stage of the decision process upon learning something that may prompt her even to change categories. For example, a woman might buy an SUV because her friends all love theirs and she likes the looks of the new models. Once on the showroom floor, however, she may see a new minivan with great storage and fuel mileage. Suddenly, she includes minivans in her consideration set and adds two new criteria to the qualifying list.[34]

AGE AND FAMILY LIFE-CYCLE STAGE

The age and family life-cycle stage of a consumer can have a significant impact on consumer behavior. How old a consumer is generally indicates what products he or she may be interested in purchasing. Consumer tastes in food, clothing, cars, furniture, and recreation are often age related. The table in Exhibit 6.11 uses data

Exhibit 6.11

Average Annual Expenditures by Age

Item	Age					
	<25	25–34	35–44	45–54	55–64	>65
Food at home	$1,917	$2,945	$4,121	$3,807	$3,487	$2,605
Food away from home	2,015	2,694	3,238	3,173	2,715	1,558
Household furnishings and equipment	1,018	1,608	2,216	1,899	2,231	1,225
Apparel and services	1,577	2,082	2,365	2,318	1,784	957
Vehicle purchases	2,721	3,949	4,407	3,945	3,756	2,007
Entertainment	1,393	2,455	2,765	3,034	2,429	1,593
Personal care products and services	337	504	627	627	550	462

SOURCE: Bureau of Labor Statistics, 2005, by the U.S. Census Bureau

compiled by the Bureau of Labor Statistics to show the differences in spending on certain items by Americans by age.[35]

Related to a person's age is his or her place in the family life cycle. As Chapter 7 explains in more detail, the *family life cycle* is an orderly series of stages through which consumers' attitudes and behavioral tendencies evolve through maturity, experience, and changing income and status. Marketers often define their target markets in terms of family life cycle, such as "young singles," "young married with children," and "middle-aged married without children." For instance, young singles spend more than average on alcoholic beverages, education, and entertainment. New parents typically increase their spending on health care, clothing, housing, and food and decrease their spending on alcohol, education, and transportation. Households with older children spend more on food, entertainment, personal care products, and education, as well as cars and gasoline. After their children leave home, older couples spend more on vehicles, women's clothing, health care, and long-distance calls. For instance, the presence of children in the home is the most significant determinant of the type of vehicle that's driven off the new-car lot. Parents are the ultimate need-driven car consumers, requiring larger cars and trucks to haul their children and all their belongings. It comes as no surprise then that for all households with children, SUVs rank either first or second among new-vehicle purchases, followed by minivans.

Marketers should also be aware of the many nontraditional life-cycle paths that are common today and provide insights into the needs and wants of such consumers as divorced parents, lifelong singles, and childless couples. Three decades ago, married couples with children under the age of 18 accounted for about half of U.S. households. Today, such families make up only 23 percent of all households, while people living alone or with nonfamily members represent more than 30 percent. Furthermore, according to the U.S. Census Bureau, the number of single-mother households grew by 25 percent over the last decade. The shift toward more single-parent households is part of a broader societal change that has put more women on the career track. Although many marketers continue to be wary of targeting nontraditional families, Charles Schwab targeted single mothers in an advertising campaign featuring Sarah Ferguson, the Duchess of York and a divorced mom. The idea was to appeal to single mothers' heightened awareness of the need for financial self-sufficiency.[36]

PERSONALITY, SELF-CONCEPT, AND LIFESTYLE

personality
A way of organizing and grouping the consistencies of an individual's reactions to situations.

Each consumer has a unique personality. Personality is a broad concept that can be thought of as a way of organizing and grouping how an individual typically reacts to situations. Thus, personality combines psychological makeup and environmental forces. It includes people's underlying dispositions, especially their most dominant characteristics. Although personality is one of the least useful concepts in the study of consumer behavior, some marketers believe that personality influences the types and brands of products purchased. For instance, the cars, clothes, or jewelry a consumer buys may reflect one or more personality traits.

COURTESY OF THE ADVERTISING ARCHIVES

Dove's most recent marketing campaign aims to recast women's self-concept in a positive way. Women of all ages, races, and sizes have become models for the successful series of television and print advertisements, called "Campaign for Real Beauty."

Self-concept, or self-perception, is how consumers perceive themselves. Self-concept includes attitudes, perceptions, beliefs, and self-evaluations. Although self-concept may change, the change is often gradual. Through self-concept, people define their identity, which in turn provides for consistent and coherent behavior.

Self-concept combines the **ideal self-image** (the way an individual would like to be) and the **real self-image** (how an individual actually perceives himself or herself). Generally, we try to raise our real self-image toward our ideal (or at least narrow the gap). Consumers seldom buy products that jeopardize their self-image. For example, someone who sees herself as a trendsetter would only buy clothing that projects a contemporary image.

Human behavior depends largely on self-concept. Because consumers want to protect their identity as individuals, the products they buy, the stores they patronize, and the credit cards they carry support their self-image. No other product quite reflects a person's self-image as much as the car he or she drives. For example, many young consumers do not like family sedans like the Honda Accord or Toyota Camry and say they would buy one for their mom, but not for themselves. Likewise, younger parents may avoid purchasing minivans because they do not want to sacrifice the youthful image they have of themselves to their new responsibilities. To combat decreasing sales, marketers of the Nissan Quest minivan decided to reposition it as something other than a "mom mobile" or "soccer mom car." They chose the ad copy "Passion built it. Passion will fill it up," followed by "What if we made a minivan that changed the way people think of minivans?"[37]

By influencing the degree to which consumers perceive a good or service to be self-relevant, marketers can affect consumers' motivation to learn about, shop for, and buy a certain brand. Marketers also consider self-concept important because it helps explain the relationship between individuals' perceptions of themselves and their consumer behavior.

An important component of self-concept is *body image*, the perception of the attractiveness of one's own physical features. For example, individuals who have cosmetic surgery often experience significantly improved overall body image and self- concept. Moreover, a person's perception of body image can be a stronger reason for trying to lose weight than either good health or other social factors.[38] With the median age of Americans rising, many companies are introducing products and services aimed at aging baby boomers who are concerned about their age and physical appearance. Bank of America has featured Harley-riding seniors in advertisements for its private-bank marketing campaign. High-end anti-aging creams are flying off department store shelves. Te Revesz, an associate director of the research firm Find/SVP says that in order to successfully market to baby boomers, ads should speak to their self image, not their chronological age. In other words, a good baby-boom marketing strategy is one that makes a 55-year-old feel 30 again. Revesz cautions, "when it comes to boomers, anything marketing to silver hair is bad marketing."[39]

Personality and self-concept are reflected in lifestyle. A **lifestyle** is a mode of living, as identified by a person's activities, interests, and opinions. *Psychographics* is

self-concept
How consumers perceive themselves in terms of attitudes, perceptions, beliefs, and self-evaluations.

ideal self-image
The way an individual would like to be.

real self-image
The way an individual actually perceives himself or herself.

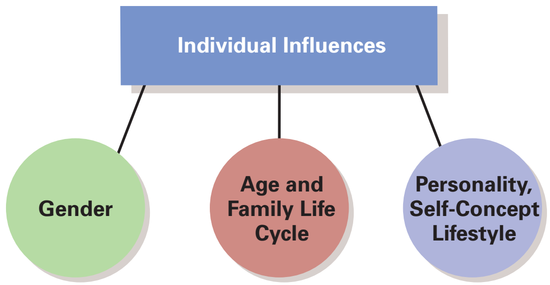
lifestyle
A mode of living as identified by a person's activities, interests, and opinions.

the analytical technique used to examine consumer lifestyles and to categorize consumers. Unlike personality characteristics, which are hard to describe and measure, lifestyle characteristics are useful in segmenting and targeting consumers. Lifestyle and psychographic analysis explicitly addresses the way consumers outwardly express their inner selves in their social and cultural environment.

Many companies now use psychographics to better understand their market segments. For many years, marketers selling products to mothers assumed that all moms were fairly homogeneous and concerned about the same things—the health and well-being of their children—and that they could all be conveniently reached with a similar message. But recent lifestyle research has shown that there are traditional, blended, and nontraditional moms, and companies like Procter & Gamble and Pillsbury are using more precise strategies to reach these different types of mothers. Psychographics is also effective with other market segments. Psychographics and lifestyle segmentation are discussed in more detail in Chapter 8.

REVIEW LEARNING OUTCOME

LO7 Identify and understand the cultural factors that affect consumer buying decisions



LO8 Psychological Influences on Consumer Buying Decisions

An individual's buying decisions are further influenced by psychological factors: perception, motivation, learning, and beliefs and attitudes. These factors are what consumers use to interact with their world. They are the tools consumers use to recognize their feelings, gather and analyze information, formulate thoughts and opinions, and take action. Unlike the other three influences on consumer behavior, psychological influences can be affected by a person's environment because they are applied on specific occasions. For example, you will perceive different stimuli and process these stimuli in different ways depending on whether you are sitting in class concentrating on the instructor, sitting outside of class talking to friends, or sitting in your dorm room watching television.

PERCEPTION

The world is full of stimuli. A stimulus is any unit of input affecting one or more of the five senses: sight, smell, taste, touch, hearing. The process by which we select, organize, and interpret these stimuli into a meaningful and coherent picture is called **perception**. In essence, perception is how we see the world around us and how we recognize that we need some help in making a purchasing decision.

People cannot perceive every stimulus in their environment. Therefore, they use **selective exposure** to decide which stimuli to notice and which to ignore. A typical consumer is exposed to more than 2,500 advertising messages a day, but notices only between 11 and 20.

The familiarity of an object, contrast, movement, intensity (such as increased volume), and smell are cues that influence perception. Consumers use these cues to identify and define products and brands. The shape of a product's—Coca-Cola's signature contour bottle, for instance—can influence perception. Color is another cue, and it plays a key role in consumers' perceptions. Packaged foods manufacturers use color to trigger unconscious associations for grocery shoppers who typically

perception
The process by which people select, organize, and interpret stimuli into a meaningful and coherent picture.

selective exposure
The process whereby a consumer notices certain stimuli and ignores others.

make their shopping decisions in the blink of an eye. When Pepsi switched from its usual blue can to a red can in a marketing campaign for the 2008 Olympics in China, they risked brand confusion with Coke products. One Pepsi drinker in China said "This is so weird. I usually just go for the blue can; it's easy to spot . . . the red can just doesn't look right." Pepsi officials say they coordinated the can with the color of China's flag to highlight their sponsorship of Team China. Pepsi had used national colors on promotional packages before, including yellow and green cans to sponsor Brazilian teams.[40]

Ampacet, a world leader in color additives for plastics, reported in 2007 that nature-inspired colors and organic values were becoming more popular as the economy and global focus shifted from the tech-boom to the bio- or eco-boom. Ecological consequences and concerns have inspired marketing initiatives such as "going green." Packaging colors like natural greens, earthy browns, and strong yellows are in, as well as metallics such as steely silver, carbon black, gold, and copper. Color researchers speculate that technological overload has led to resurgence in the appreciation of simplistic luxury. Color names for fabrics and makeup reflect that trend with names such as Grounded, Champagne Chic, and Serene Blue.[41]

Consumers' perceptions may also depend on the stimuli's vividness or shock value. Graphic warnings of the hazards associated with a product's use are perceived more readily and remembered more accurately than less vivid warnings or warnings that are written in text. "Sexier" ads excel at attracting the attention of younger consumers. Companies like Calvin Klein and Guess use sensuous ads intended to create a fantasy or mood that captures the attention of their target audience. Fragrance advertisements often emphasize the "outcome" of wearing their product, often promising a role transformation for the wearer. David Rubin, brand development director for Axe deodorant, says Axe's theme from the very start has been "giving guys an edge in the mating game."[42]

selective distortion
A process whereby a consumer changes or distorts information that conflicts with his or her feelings or beliefs.

selective retention
A process whereby a consumer remembers only that information that supports his or her personal beliefs.

Two other concepts closely related to selective exposure are selective distortion and selective retention. Selective distortion occurs when consumers change or distort information that conflicts with their feelings or beliefs. For example, suppose a college student buys a Sonicblue Rio MP3 player. After the purchase, if the student gets new information about an alternative brand, such as an Apple iPod, he or she may distort that information to make it more consistent with his or her prior view that the Sonicblue Rio is just as good as the iPod, if not better. Business travelers who fly often may distort or discount information about airline crashes because they must use air travel constantly in their jobs.

Selective retention is remembering only information that supports personal feelings or beliefs. The consumer forgets all information that may be inconsistent. After reading a pamphlet that contradicts one's political beliefs, for instance, a person may forget many of the points outlined in it. Similarly, consumers may see a news report on suspected illegal practices by their favorite retail store, but soon forget the reason the store was featured on the news.

Which stimuli will be perceived often depends on the individual. People can be exposed to the same stimuli under identical conditions but perceive them very differently. For example, two people viewing a TV commercial may have different interpretations of the advertising message. One person may be thoroughly engrossed by the message and become highly motivated to buy the product. Thirty seconds after the ad ends, the second person may not be able to recall the content of the message or even the product advertised.

Marketing Implications of Perception

Marketers must recognize the importance of cues, or signals, in consumers' perception of products. Marketing managers first identify the important attributes, such as price or quality, that the targeted consumers want in a product and then design signals to communicate these attributes. For example, consumers will pay more for candy in expensive-looking foil packages. But shiny labels on wine bottles signify cheaper wines; dull labels indicate more expensive wines. Marketers also often use price as a signal to consumers that the product is of higher quality than competing products. Gibson Guitar Corporation briefly cut prices on many of its guitars to compete with Japanese rivals Yamaha and Ibanez, but found that it sold more guitars when it charged more for them. Consumers perceived that the higher price indicated a better quality instrument.[43]

Of course, brand names send signals to consumers. The brand names of Close-Up toothpaste, DieHard batteries, and Caress moisturizing soap, for example, identify important product qualities. Names chosen for search engines and sites on the Internet, such as Yahoo!, Amazon.com, and Excite, are intended to convey excitement, intensity, and vastness. Companies may even change their names to send a message to consumers. As today's utility companies increasingly enter unregulated markets, many are shaking their stodgy "Power & Light & Electric" names in favor of those that tell consumers they aren't just about electricity anymore, such as Reliant Resources, Entergy, and Cinergy.

Consumers also associate quality and reliability with certain brand names. Companies watch their brand identity closely, in large part because a strong link has been established between perceived brand value and customer loyalty. Brand names that consistently enjoy high perceived value from consumers include Kodak, Disney, National Geographic, Mercedes-Benz, and Fisher-Price. Naming a product after a place can also add perceived value by association. Brand names using the words Santa Fe, Dakota, or Texas convey a sense of openness, freedom, and youth, but products named after other locations might conjure up images of pollution and crime.

Marketing managers are also interested in the *threshold level of perception*: the minimum difference in a stimulus that the consumer will notice. This concept is sometimes referred to as the "just-noticeable difference." For example, how much would Apple have to drop the price of its iPod Shuffle before consumers recognized it as a bargain—$25? $50? or more? One study found that the just-noticeable difference in a stimulus is about a 20 percent change. For example, consumers will likely notice a 20 percent price decrease more quickly than a 15 percent decrease. This principle can be applied to other marketing variables as well, such as package size or loudness of a broadcast advertisement.[44]

Another study showed that the bargain-price threshold for a name brand is lower than that for a store brand. In other words, consumers perceive a bargain more readily when stores offer a small discount on a name-brand item than when they offer the same discount on a store brand; a larger discount is needed to achieve a similar effect for a store brand.[45] Researchers also found that for low-cost grocery items, consumers typically do not see past the second digit in the price. For instance, consumers do not perceive any real difference between two comparable cans of tuna, one priced at $1.52 and the other at $1.59, because they ignore the last digit.[46]

Besides changing such stimuli as price, package size, and volume, marketers can change the product or attempt to reposition its image. But marketers must be careful when adding features. How many new services will discounter Target Stores need to add before consumers perceive it as a full-service department store? How many sporty features will General Motors have to add to a basic two-door sedan before consumers start considering it a sports car?

Marketing managers who intend to do business in global markets should be aware of how foreign consumers perceive their products. For instance, in Japan, product labels are often written in English or French, even though they may not translate into anything meaningful. Many Japanese associate foreign words on product labels with the exotic, and the expensive, believing they indicate high quality.

Marketers have often been suspected of sending advertising messages subconsciously to consumers in what is known as *subliminal perception*. The controversy began when a researcher claimed to have increased popcorn and Coca-Cola sales at a movie theater after flashing "Eat popcorn" and "Drink Coca-Cola" on the screen every five seconds for 1/300th of a second, although the audience did not consciously recognize the messages. Almost immediately consumer protection groups became concerned that advertisers were brainwashing consumers, and this practice was pronounced illegal in California and Canada. Although the researcher later admitted to making up the data and scientists have been unable to replicate the study since, consumers are still wary of hidden messages that advertisers may be sending.

MOTIVATION

By studying motivation, marketers can analyze the major forces influencing consumers to buy or not buy products. When you buy a product, you usually do so to fulfill some kind of need. These needs become motives when aroused sufficiently. For instance, suppose this morning you were hungry before class and needed to eat something. In response to that need, you stopped at McDonald's for an Egg McMuffin. In other words, your hunger motivated you to stop at McDonald's. Motives are the driving forces that cause a person to take action to satisfy specific needs.

motive
A driving force that causes a person to take action to satisfy specific needs.

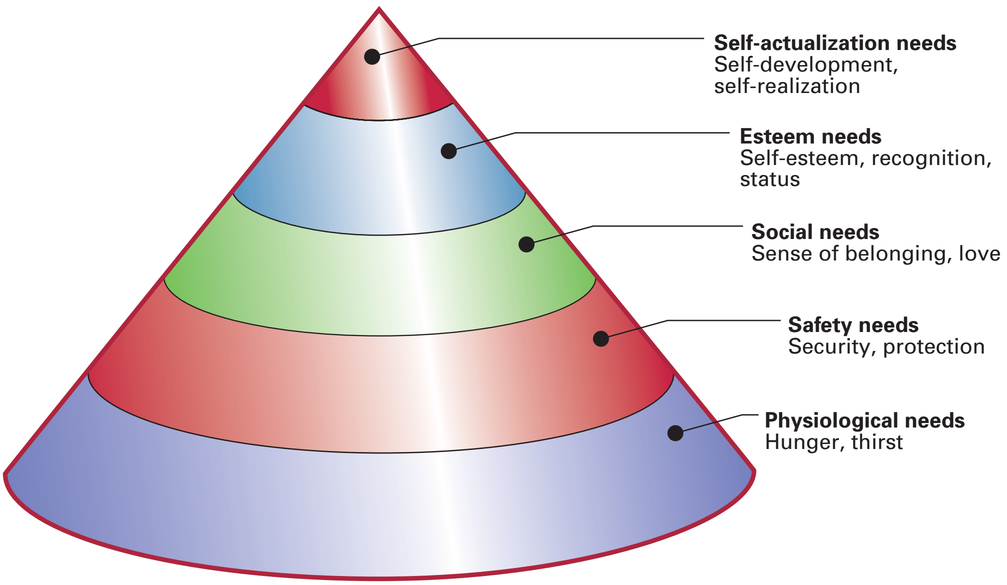
Maslow's hierarchy of needs
A method of classifying human needs and motivations into five categories in ascending order of importance: physiological, safety, social, esteem, and self-actualization.

Why are people driven by particular needs at particular times? One popular theory is Maslow's hierarchy of needs, shown in Exhibit 6.12, which arranges needs in ascending order of importance: physiological, safety, social, esteem, and self-actualization. As a person fulfills one need, a higher level need becomes more important.

The most basic human needs are *physiological*—that is the needs for food, water, and shelter. Because they are essential to survival, these needs must be satisfied first. Ads showing a juicy hamburger or a runner gulping down Gatorade after a marathon are examples of appeals to satisfy the physiological needs of hunger and thirst.

Safety needs include security and freedom from pain and discomfort. Marketers sometimes appeal to consumers' fears and concerns about safety to sell their products. For example, aware of the aging population's health fears, the retail medical imaging centers Heart Check America and HealthScreen America advertise that they offer consumers a full body scan for early detection of health problems like coronary disease and cancer. On the other hand, some companies or industries advertise to allay consumer fears. For example, in the wake of the September 11 terrorist attacks, the airline industry conducted an image campaign to reassure consumers about the safety of air travel.[47]

Exhibit 6.12
Maslow's Hierarchy of Needs



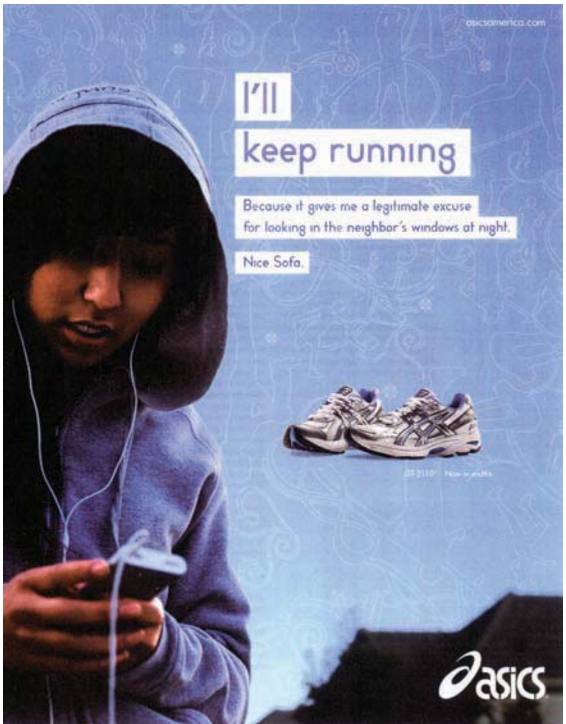
After physiological and safety needs have been fulfilled, *social needs*—especially love and a sense of belonging—become the focus. Love includes acceptance by one's peers, as well as sex and romantic love. Marketing managers probably appeal more to this need than to any other. Ads for clothes, cosmetics, and vacation packages suggest that buying the product can bring love. The need to belong is also a favorite of marketers, especially those marketing products to teens.

Teens consider the iPod to be not only their favorite brand but also as defining their generation. Other such brands include American Eagle Outfitters, Axe, Baby Phat, Facebook, Google, Hollister, MTV, MySpace, Vans, and YouTube. The VP of Research at MTV says marketers need to understand a new dynamic in the "millennial generation" consumer. The relationship this generation has with their parents is completely different from previous generations'. Parents can be best friends. Brands that focus too heavily on "influential" teens, can overlook the fact that parents can be the biggest influencer on this age group, especially when it comes to big-ticket items.[48]

Love is acceptance without regard to one's contribution. Esteem is acceptance based on one's contribution to the group. *Self-esteem needs* include self-respect and a sense of accomplishment. Esteem needs also include prestige, fame, and recognition of one's accomplishments. Mont Blanc pens, Mercedes-Benz automobiles, and Neiman Marcus stores all appeal to esteem needs. Most high-end spas and health clubs appeal to consumers' self-esteem needs. Like exclusive country clubs, clubs such as Chicago's East Bank Club are designed to make members feel proud of their commitment to fitness while also giving them a sense of social accomplishment. In fact, the clubs can be so effective that even during an economic recession, patrons will not give up their membership because doing so would be a public admission of financial problems.[49]

learning
A process that creates changes in behavior, immediate or expected, through experience and practice.

Asian consumers, in particular, are strongly motivated by status and appearance. Asians tend to be conscious of their place in a group, institution, or society as a whole. The importance of gaining social recognition makes Asians some of the most image-conscious consumers in the world. Status-conscious Asians will not hesitate to spend freely on premium brands, such as BMW, Mercedes-Benz, and the best Scotch whiskey and French cognac. Indeed, marketers of luxury products such as Gucci, Louis Vuitton, and Prada find that demand for their products is so strong among image-conscious consumers that their sales are generally unaffected by economic downturns. In some cases, companies have been able to make up for sluggish European and U.S. sales by raising prices and volume in Asia.



More than one motive may drive a consumer's purchase. This Asics advertisement encourages consumers to buy sneakers by highlighting an unconventional benefit of running instead of a more traditional one, like exercise.

The highest human need is *self-actualization*. It refers to finding self-fulfillment and self-expression, reaching the point in life at which "people are what they feel they should be." Maslow felt that very few people ever attain this level. Even so, advertisements may focus on this type of need. For example, American Express ads suggest that acquiring its card is one of the highest attainments in life. Microsoft appealed to consumers' needs for self-actualization when it chose "Your Potential Our Passion" as the Windows XP slogan. Similarly, the U.S. Army changed its slogan from "Be all that you can be" to "Army of One," and the U.S. Navy adopted a slogan urging young people to "Accelerate Your Life."

LEARNING

Almost all consumer behavior results from **learning**, which is the process that creates changes in behavior through experience and practice. It is not possible to observe learning directly, but we can infer when it has occurred by a person's actions. For example, suppose you see an advertisement for a new and improved cold medicine. If you go to the store that day and buy that remedy, we infer that you have learned something about the cold medicine.

There are two types of learning: experiential and conceptual. *Experiential learning* occurs when an experience changes your behavior. For example, if the new cold medicine does not relieve your symptoms, you may not buy that brand again. *Conceptual learning*, which is not acquired through direct experience, is the second type of learning. Assume, for example, that you are standing at a soft drink machine and notice a new diet flavor with an artificial sweetener. Because someone has told you that diet beverages leave an aftertaste, you choose a different drink. You have learned that you would not like this new diet drink without ever trying it.

Reinforcement and repetition boost learning. Reinforcement can be positive or negative. If you see a vendor selling frozen yogurt (stimulus), buy it (response), and enjoy it (reward), your behavior has been positively reinforced. On the other hand, if you buy a new flavor of yogurt and it does not taste good (negative reinforcement), you will not buy that flavor of yogurt again (response). Without positive or negative reinforcement, a person won't be motivated to repeat the behavior pattern or to avoid it. Thus, if a new brand evokes neutral feelings, some marketing activity, such as a price change or an increase in promotion, may be required to induce further consumption. Learning theory is helpful in reminding marketers to take concrete and timely actions to reinforce desired consumer behavior.

Repetition is a key strategy in promotional campaigns because it can lead to increased learning. Most marketers use repetitious advertising so that consumers will learn what their unique advantage is over the competition. Generally, to heighten learning, advertising messages should be spread out over time rather than clustered together.

stimulus generalization
A form of learning that occurs when one response is extended to a second stimulus similar to the first.

A related learning concept useful to marketing managers is stimulus generalization. In theory, **stimulus generalization** occurs when one response is extended to a second stimulus similar to the first. Marketers often use a successful, well-known brand name for a family of products because it gives consumers familiarity with and knowledge about each product in the family. Such brand-name families spur the introduction of new products and facilitate the sale of existing items. Jell-O frozen pudding pops rely on the familiarity of Jell-O gelatin; Clorox bathroom cleaner relies on familiarity with Clorox bleach; and Dove shampoo relies on familiarity with Dove soap. Microsoft entered the video game industry, hoping that the Microsoft brand would guarantee sales for the Xbox. Initial response to the Xbox was strong based on Microsoft's reputation. Since then, Microsoft has worked hard to be successful in an industry dominated by other brand giants like Sony and Nintendo. The latest generation Xbox 360 Elite has jaw-dropping high-definition graphics, unmatched online play, and compelling digital entertainment; it plays music and movies stored in an array of devices, including MP3 players, and displays photos from digital cameras. Branding is examined in more detail in Chapter 10.

Another form of stimulus generalization occurs when retailers or wholesalers design their packages to resemble well-known manufacturers' brands. Such imitation often confuses consumers, who buy the imitation thinking it's the original. U.S. manufacturers in foreign markets have sometimes found little, if any, brand protection. BMW and Daimler-Chrysler recently sued Chinese car manufacturers for creating near-exact replicas of their cars. Cosmetics giant L'Oreal, maker of Gucci and other luxury brands, is threatening legal action against eBay unless the auction site cracks down on sales of counterfeit L'Oreal products on its site. DVD piracy is rampant in China; so much so that special DVD-counterfeit-sniffing dogs have become a common sight in international airports. After the terrorist attacks of 9-11 and subsequent stepped-up security regulations, authentication technologies have been used successfully in identifying fake passports, currency, and credit cards. Those same technologies—and others, such as embedded microchips, holographic symbols, and tamper-proof packaging—are now being used in everyday products such as clothing, footwear, computers, cell phones, video games, jewelry, software, pharmaceuticals, and medical devices, making it easier for importers and retailers to spot fakes.[50]

stimulus discrimination
A learned ability to differentiate among similar products.

belief
An organized pattern of knowledge that an individual holds as true about his or her world.

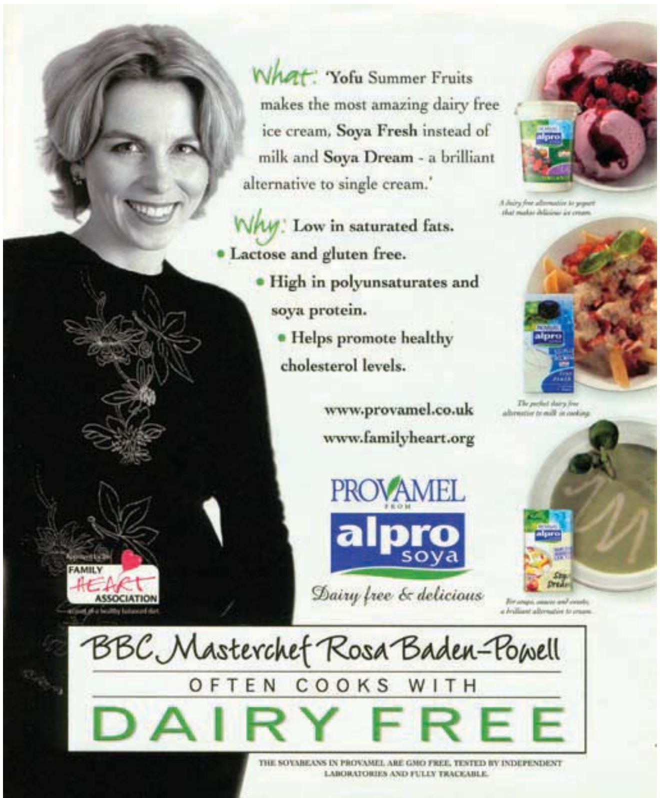
attitude
A learned tendency to respond consistently toward a given object.

The opposite of stimulus generalization is **stimulus discrimination**, which means learning to differentiate among similar products. Consumers may perceive one product as more rewarding or stimulating. For example, some consumers prefer Coca-Cola and others prefer Pepsi. Many insist they can taste a difference between the two brands.

With some types of products—such as aspirin, gasoline, bleach, and paper towels—marketers rely on promotion to point out brand differences that consumers would otherwise not recognize. This process, called *product differentiation*, is discussed in more detail in Chapter 8. Usually, product differentiation is based on superficial differences. For example, Bayer tells consumers that it's the aspirin "doctors recommend most."

BELIEFS AND ATTITUDES

Beliefs and attitudes are closely linked to values. A **belief** is an organized pattern of knowledge that an individual holds as true about his or her world. A consumer may believe that Sony's camcorder makes the best home videos, tolerates hard use, and is reasonably priced. These beliefs may be based on knowledge, faith, or hearsay. Consumers tend to develop a set of beliefs about a product's attributes and then, through these beliefs, form a *brand image*—a set of beliefs about a particular brand. In turn, the brand image shapes consumers' attitudes toward the product.



To increase sales, a company must change negative attitudes about its product held by those who are not buying it. One way to accomplish this is to change the beliefs about the product's attributes, such as taste. This ad for soy-based products attempts to do just that by concluding the list of healthful advantages with the tag line "Dairy free & delicious".

An **attitude** is a learned tendency to respond consistently toward a given object, such as a brand. Attitudes rest on an individual's value system, which represents personal standards of good and bad, right and wrong, and so forth; therefore, attitudes tend to be more enduring and complex than beliefs.

For example, consider the differing attitudes of consumers around the world toward the practice of purchasing on credit. Americans have long been enthusiastic about charging goods and services and are willing to pay high interest rates for the privilege of postponing payment. To many European consumers, doing what amounts to taking out a loan—even a small one—to pay for anything seems absurd. Germans especially are reluctant to buy on credit. Italy has a sophisticated credit and banking system well suited to handling credit cards, but Italians prefer to carry cash, often huge wads of it. Although most Japanese consumers have credit cards, card purchases amount to less than 1 percent of all consumer transactions. The Japanese have long looked down on credit purchases, but acquire cards to use while traveling abroad.

If a good or service is meeting its profit goals, positive attitudes toward the product merely need to be reinforced. If the brand is not succeeding, however, the marketing manager must strive to change target consumers' attitudes toward it. Changes in attitude tend to grow out of an individual's attempt to reconcile long-held values with a constant stream of new information. This change can be accomplished in three ways: changing beliefs about the brand's attributes, changing the relative importance of these beliefs, and adding new beliefs.

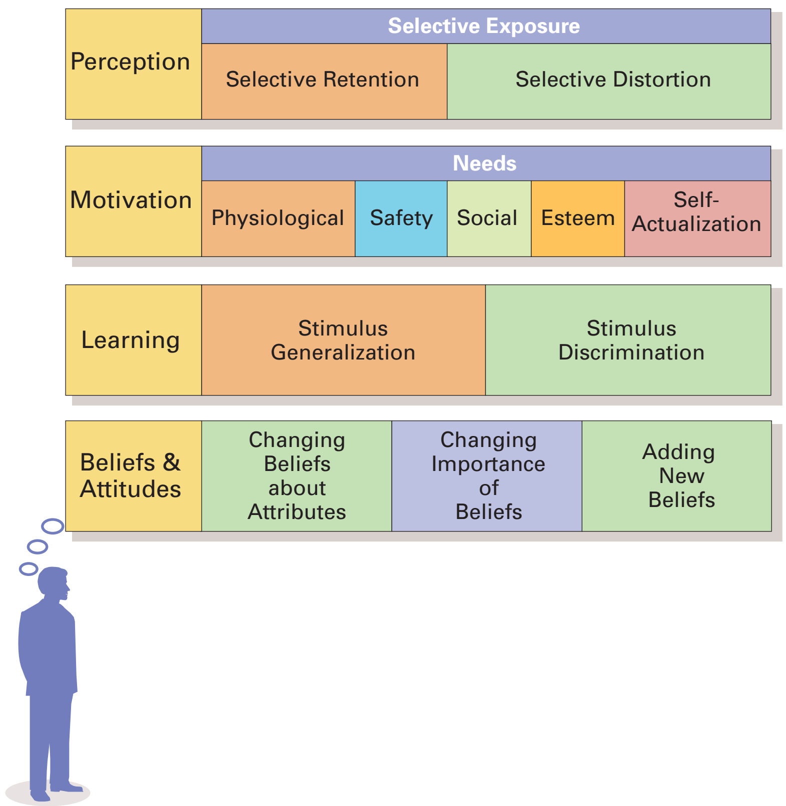
Changing Beliefs about Attributes

The first technique is to turn neutral or negative beliefs about product attributes into positive ones. For example, many consumers believe that it is easier and cheaper to take traditional film to be developed than it is to print their own digital photos. To change this belief, Kodak has begun setting up kiosks in retail outlets that allow consumers to print their digital photos. The kiosks eliminate the need for consumers to purchase their own high-quality printer.

Changing beliefs about a service can be more difficult because service attributes are intangible. Convincing consumers to switch hairstylists or lawyers or go to a mall dental clinic can be much more difficult than getting them to change brands of razor blades. Image, which is also largely intangible, significantly determines service patronage. For example, GE has created a new light bulb, a compact fluorescent lamp (CFL), that uses 1/3 the energy of a traditional bulb, lasts nearly 10 times longer, and can save up to $30 in energy costs over its lifetime. GE's new campaign urges the use of its new bulb by appealing to Americans' burgeoning ecological awareness, while exhibiting its own "care" for the world's resources. How could the consumer possibly resist when GE has made it so easy to participate? If every American swapped one standard bulb for a CFL, it would collectively prevent burning 30 billion pounds of coal and remove two million cars worth of greenhouse gas emissions from the atmosphere.[51] Service marketing is explored in detail in Chapter 12.

REVIEW LEARNING OUTCOME

LO8 Identify and understand the psychological factors that affect consumer buying decisions



Changing the Importance of Beliefs

The second approach to modifying attitudes is to change the relative importance of beliefs about an attribute. Cole Haan, originally a men's shoe outfitter, used boats and cars in its ads for years to associate the brand with active lifestyles, an important attribute for men. Now that it sells women's products, such as handbags and shoes, some of its ads use models and emphasize the products' appearence, an important attribute for women. The company hopes the ads will change customers' perceptions and beliefs that it only sells men's products.[52]

Marketers can also emphasize the importance of some beliefs over others. For example, Chrysler's Jeep unit positions itself as a rugged vehicle, but promotes its luxury features. The newest Grand Cherokees have even more off-road capability, but very few owners ever take them off-road. Luxury features include a climate-control system with infrared beams that track drivers' and passengers' skin temperature to automatically adjust air conditioning and heat, his and her key rings that remember settings for power seats and mirrors, a system to reprogram radio stations for different drivers, and many other comforts.

Adding New Beliefs

The third approach to transforming attitudes is to add new beliefs. Although changes in consumption patterns often come slowly, cereal marketers are betting that consumers will eventually warm up to the idea of cereal as a snack. A print ad for General Mills's Cookie-Crisp cereal features a boy popping the sugary nuggets into his mouth while he does his homework. Koch Industries, the manufacturer of Dixie paper products, is also attempting to add new beliefs about the uses of its paper plates and cups with an advertising campaign aimed at positioning its product as a "home cleanup replacement." Commercials pitch Dixie paper plates as an alternative to washing dishes after everyday meals.

U.S. companies attempting to market their goods overseas may need to help consumers add new beliefs about a product in general. Coca-Cola and PepsiCo have both struggled to sell their diet cola brands to consumers in India partly because diet foods of any kind are a new concept in that country, where malnutrition was widespread not too many years ago. Indians also have a deep-rooted attitude that anything labeled "diet" is meant for a sick person, such as a diabetic. As a general rule, most Indians aren't diet-conscious, preferring food prepared in the traditional manner that tastes good. Indians are also suspicious of the artificial sweeteners used in diet colas. India's Health Ministry has required warning labels on cans and bottles of Diet Coke and Diet Pepsi saying "Not Recommended for Children."[53]

---

5 < number of factors determining the 3 types of consumer buying decisions

Kellogg's cereal advertising budget > **$206 million**

4% < projected growth rate for the total U.S. population

projected growth rate for the population of African-American women > **8%**

73 < percentage American Hispanics reached by Univision Radio

reported worth of Nike's endorsement deal with LeBron James > **$1,000**

reported worth of Nike's endorsement deal with LeBron James > **$90 million**

28 million < number of registered users of the online community Piczo

number of blogs monitored by Technorati > **35.3 million**

Review and Applications

LO 1 **Explain why marketing managers should understand consumer behavior.** Consumer behavior describes how consumers make purchase decisions and how they use and dispose of the products they buy. An understanding of consumer behavior reduces marketing managers' uncertainty when they define a target market and design a marketing mix.

1.1 The type of decision making a consumer uses for a product does not necessarily remain constant. Why? Support your answer with an example from your own experience.

LO 2 **Analyze the components of the consumer decision-making process.** The consumer decision-making process begins with need recognition, when stimuli trigger awareness of an unfulfilled want. If additional information is required to make a purchase decision, the consumer may engage in an internal or external information search. The consumer then evaluates the additional information and establishes purchase guidelines. Finally, a purchase decision is made.

ONLINE

2.1 Visit Carpoint's Web site at **http://autos.msn.com/home/carresearch.aspx? src=msnhp.** How does the site assist consumers in the evaluation stage of choosing a new car? Develop your own hypothetical evoked set of three or four car models and present your comparisons. Which vehicle attributes would be most important in your purchase decision?

LO3 **Explain the consumer's postpurchase evaluation process.** Consumer postpurchase evaluation is influenced by prepurchase expectations, the prepurchase information search, and the consumer's general level of self-confidence. Cognitive dissonance is the inner tension that a consumer experiences after recognizing a purchased product's disadvantages. When a purchase creates cognitive dissonance, consumers tend to react by seeking positive reinforcement for the purchase decision, avoiding negative information about the purchase decision, or revoking the purchase decision by returning the product.

WRITING

3.1 Recall an occasion when you experienced cognitive dissonance about a purchase. In a letter to a friend, describe the event and explain what you did about it.

LO4 **Identify the types of consumer buying decisions and discuss the significance of consumer involvement.** Consumer decision making falls into three broad categories. First, consumers exhibit routine response behavior for frequently purchased, low-cost items that require very little decision effort; routine response behavior is typically characterized by brand loyalty. Second, consumers engage in limited decision making for occasional purchases or for unfamiliar brands in familiar product categories. Third, consumers practice extensive decision making when making unfamiliar, expensive, or infrequent purchases. High-involvement decisions usually include an extensive information search and a thorough evaluation of alternatives. In contrast, low-involvement decisions are characterized by brand loyalty and a lack of personal identification with the product. The main factors affecting the level of consumer involvement are previous experience, interest, perceived risk of negative consequences (financial, social, and psychological), situation, and social visibility.

4.1 Describe the three categories of consumer decision-making behavior. Name typical products for which each type of consumer behavior is used.

ONLINE

4.2 Describe the level of involvement and the involvement factors likely to be associated with buying a new computer. Do you think Apple's Web site at **http://www.apple.com** simplifies or complicates the process for the average consumer? Explain.

LO5 **Identify and understand the cultural factors that affect consumer buying decisions.** Cultural influences on consumer buying decisions include culture and values, subculture, and social class. Culture is the essential character of a society that distinguishes it from other cultural groups. The underlying elements of every culture are the values, language, myths, customs, rituals, laws, and artifacts, or products, which are transmitted from one generation to the next. The most defining element of a culture is its values—the enduring beliefs shared by a society that a specific mode of conduct is personally or socially preferable to another mode of conduct. A culture can be divided into subcultures on the basis of demographic characteristics, geographic regions, national and ethnic background, political beliefs, and religious beliefs. Subcultures share elements of the overall culture as well as cultural elements unique to their own group. A social class is a group of people who are considered nearly equal in status or community esteem, who regularly socialize among themselves both formally and informally, and who share behavioral norms.

WRITING

5.1 You are a new marketing manager for a firm that produces a line of athletic shoes to be targeted to the college student subculture. In a memo to your boss, list some product attributes that might appeal to this subculture and the steps in your customers' purchase processes, and recommend some marketing strategies that can influence their decision.

LO6 **Identify and understand the social factors that affect consumer buying decisions.** Social factors include such external influences as reference groups, opinion leaders, and family. Consumers seek out others' opinions for guidance on new products or services and products with image-related attributes or because attribute information is lacking or uninformative. Consumers may use products or brands to identify with or become a member of a reference group. Opinion leaders are members of reference groups who influence others' purchase decisions. Family members also influence purchase decisions; children tend to shop in similar patterns as their parents.

6.1 Family members play many different roles in the buying process: initiator, influencer, decision maker, purchaser, and consumer. Identify the person in your family who might play each of these roles in the purchase of a dinner at Pizza Hut, a summer vacation, Froot Loops breakfast cereal, an Abercrombie & Fitch sweater, golf clubs, an Internet service provider, and a new car.

LO7 **Identify and understand the individual factors that affect consumer buying decisions.** Individual factors that affect consumer buying decisions include gender; age and family life-cycle stage; and personality, self-concept, and lifestyle. Beyond obvious physiological differences, men and women differ in their social and economic roles, and that affects consumer buying decisions. How old a consumer is generally indicates what products he or she may be interested in purchasing. Marketers often define their target markets in terms of consumers' life-cycle stage, following changes in consumers' attitudes and behavioral tendencies as they mature. Finally, certain products and brands reflect consumers' personality, self-concept, and lifestyle.

7.1 Assume you are involved in the following consumer decision situations: (a) renting a DVD to watch with your roommates, (b) choosing a fast-food restaurant to go to with a new friend, (c) buying a popular music compact disc, (d) buying jeans to wear to class. List the individual factors that would influence your decision in each situation and explain your responses.

LO8 **Identify and understand the psychological factors that affect consumer buying decisions.** Psychological factors include perception, motivation, learning, values, beliefs, and attitudes. These factors allow consumers to interact with the world around them, recognize their feelings, gather and analyze information, formulate thoughts and opinions, and take action. Perception allows consumers to recognize their consumption problems. Motivation is what drives consumers to take action to satisfy specific consumption needs. Almost all consumer behavior results from learning, which is the process that creates changes in behavior through experience. Consumers with similar beliefs and attitudes tend to react alike to marketing-related inducements.

8.1 How do beliefs and attitudes influence consumer behavior? How can negative attitudes toward a product be changed? How can marketers alter beliefs about a product? Give some examples of how marketers have changed negative attitudes about a product or added or altered beliefs about a product.

Key Terms

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consumer decision-making process	166
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Exercises

APPLICATION EXERCISE

Principles of consumer behavior are evident in many areas of marketing. Perhaps the easiest place to see this critical foundation of marketing activity is in print ads.[54]

Activities

1. Review the main concepts in this chapter and create a checklist that itemizes them. Then, comb through your favorite magazines and newspapers for advertisements that illustrate each

concept. To get a wide variety of ads, you will need to look through several magazines. If you don't have many magazines at your disposal, go to the campus library periodical room. Photocopy the ads you select to support this chapter.

2. Because pictures can help reinforce understanding, consider doing this exercise for each chapter in the book. At the end of the semester, you will have a portfolio of ads that illustrate the concepts in the entire book, which can help you study. Simply look through your portfolio and try to recall the concepts at work in each advertisement. This exercise can be a prelude to a longer study session for comprehensive exams.

ETHICS

ETHICS EXERCISE

EyeOnU operates a Web filter service for public schools and libraries to protect students from inappropriate material on the Internet. Like the industry as a whole, the company's market share has been stagnant for the past two years. Looking for new sources of revenue, the company is considering selling the data it has collected about student surfing habits to marketers trying to learn more about students' behavior on the Web. The data are anonymous, but privacy advocates are concerned about the precedent of selling information about children to marketers.

Questions

1. What should EyeOnU do? Should it protect the student's data, or should it take the opportunity to create new revenues?
2. Visit the COPPA site dedicated to distributing information about the Children's Online Privacy Protection Act at **http://www.coppa.org/comply.htm**. Then write a brief paragraph on the responsibilities a Web site operator has to protect children's privacy and safety online and how that relates to EyeOnU's dilemma.

© AP PHOTO/ JEFF ROBERSON

Case Study: Ethel's Chocolate Lounges

BACK TO THE FUTURE? CHOCOLATE LOUNGES TASTE SWEET SUCCESS

The chocolate house dates back to seventeenth-century London, when members of society's elite would gather in luxurious surroundings to relax and sip hot chocolate. Later, Europeans expanded on that idea and developed solid chocolate treats that sold in upscale boutiques. Lacking the resources and economy of established continentals, bootstrapping American settlers pioneered the development of cheaper chocolate bars for the masses.

Centuries have passed, however, and mass-produced chocolate now bores the American palate. The U.S. chocolate industry has experienced growth of less than 3 percent since the turn of the millennium, and the lack of industry innovation has left a bad taste in chocolate purveyors' mouths, too. Enter Ethel's Chocolate Lounges, named in honor of the matriarch of the Mars family, who founded the candy company with her husband Frank in 1911.

Now Ethel Mars's name adorns the signs at the company's latest attempt to breathe fresh life into chocolate. Aware that chocolate sales at upscale retail outlets, like Godiva and Starbucks grew by nearly 20 percent from 2002 to 2004, Mars opened Ethel's Chocolate Lounge in the Lincoln Park neighborhood of Chicago in April 2005. More Ethel's Lounges have opened since then, and the chic chocolate houses are Mars's bet that well-heeled and sweet-toothed consumers will take to premium chocolate the same way that well-to-do coffee lovers flock to Starbucks for high-priced java. Ethel's Lounges are designed to coddle patrons in the lap of luxury, but Mars president John Haugh maintains that what makes Ethel's special is that it offers "approachable gourmet chocolate." In other words, you don't have to be a millionaire to enjoy the sweet taste of the good life.

Prices are not for everyone's wallet, however. Truffles and Tea for Two, which features all 11 of Ethel's truffles served on a silver platter, sells for $15. Chocolates and Cocoa for Two includes two cocoas and 10 pieces of chocolate for $18, and a box of 48 chocolates is $42. Five "Collections" offer over 50 individual chocolates that sell for between $.90 and $1.50.

Supporting Haugh's claim of approachability, though, the menus at Ethel's feature icons and descriptions of the chocolates' contents so that customers won't experience an unwanted surprise. A multitude of hot and cold beverages entice visitors to extend their stays.

But it's not just the chocolate that makes Ethel's such a desirable destination. Advertising describes Ethel's as "a place for chocolate and chitchat." Generously stuffed pink couches with brown accents combine upscale modern and traditional looks to give the stores a hip and classy feel. For those who don't immediately get it, a sign behind the counter reads, "Chocolate is the new black." The stores' appeal is their relaxing ambience and neighborhood vibe—like a modern American coffeehouse, these shops encourage socializing and extended lounging. The effect is carefully planned. Mars's research revealed that even calorie-conscious consumers will splurge for the good stuff as long as a broader social experience comes with it.

Parallels to the Starbucks-led American coffee revival are obvious and inescapable. Confectionary industry insiders note that chocolate cafés are taking hold, and research confirms their belief. Datamonitor, a research firm specializing in trend identification, described chocolate as "the new coffee" on its list of the top ten trends to watch in 2006. The popularity of the Chocolate Bar in New York, billed as a "candy store for grown-ups," and South Bend Chocolate's ten chocolate cafés shows that the trend is for real. Even some Hershey's stores now offer seating for patrons.

Joan Steuer, president of Chocolate Marketing, claims that, for women, enjoying chocolate in a luxurious lounge is like taking a candle-lit bubble bath. She notes, too, that much of the appeal is that the experience is testimony to the person's upward mobility. It's a perfect way to cater to the American desire to have the best that money can buy.[55]

Questions

1. What type of consumer buying decision best describes the choice to indulge at Ethel's?
2. List the factors that might influence a consumer to spend money and time at Ethel's. Which factor do you think will motivate a consumer the most? Why?
3. Review the core American values in Exhibit 6.5. Which value does the Ethel's experience appeal to most? Explain.

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Company Clips

READYMADE—DO-IT-YOURSELF

In 2001 when Grace Hawthorne, CEO, and Shoshana Berger, Editor-in-Chief, came up with their idea for ReadyMade, there were no other publications with their unique do-it-yourself (DIY) theme. ReadyMade was to be a magazine about fun and creative projects for the home. Since its development, the bimonthly magazine has enjoyed a loyal subscriber base and continues to gain readership across the country. All issues include numerous do-it-yourself (DIY) projects, each rated by their level of difficulty, as well as several feature articles exploring the latest in innovation and design. In this video, pay attention to ReadyMade's methods as they launched their magazine. Note also how ReadyMade uses its knowledge of its consumer base to tailor the product.

Questions

1. While the ReadyMade magazine was still in the design stages, very little research was done to determine whether an interested market existed. Did this adversely affect the magazine as it moved forward to publication? Explain.
2. How does the cover of ReadyMade magazine reflect the principles of packaging design as influenced by the known behaviors of its consumers?
3. To what extent does ReadyMade rely on opinion leaders to promote the magazine? Is this a successful tactic?

Marketing & You Results

High scores suggest that you tend to shop for value, whereas lower scores indicate compulsive buying, or excessive shopping relative to your disposable income. Lower scores also suggest that you may use excessive shopping to deal with undesirable moods or negative feelings. Even though your mood might improve afterward, beware; the change is temporary, compulsive shopping behavior is very difficult to stop, and can have painful consequences.

ANATOMY OF A **Buying Decision**

Car

For a high-involvement purchase, such as buying a car, a consumer typically practices extensive decision making. Several factors ultimately affect her buying decision.

Advice from her reference group

Example of opinion leader

Social factors:

Before deciding to buy a car, this woman may seek out others' opinions or observe what others purchase.

Self-concept

Lifestyle

Individual factors:

Her buying decision will be influenced by her personality, self-concept, and lifestyle.

"Should I try a new brand, or stick with the familiar one?"

Attitude

Psychological factors:

The consumer's perception, motivation, learning, values, beliefs, and attitudes will influence her decision on which car to buy, too.

CHAPTER 7

Business Marketing

Learning Outcomes

- LO 1 Describe business marketing
- LO 2 Describe the role of the internet in business marketing
- LO 3 Discuss the role of relationship marketing and strategic alliances in business marketing
- LO 4 Identify the four major categories of business market customers
- LO 5 Explain the North American industry classification system
- LO 6 Explain the major differences between business and consumer markets
- LO 7 Describe the seven types of business goods and services
- LO 8 Discuss the unique aspects of business buying behavior

LO 1
What Is Business Marketing?

business marketing
The marketing of goods and services to individuals and organizations for purposes other than personal consumption.

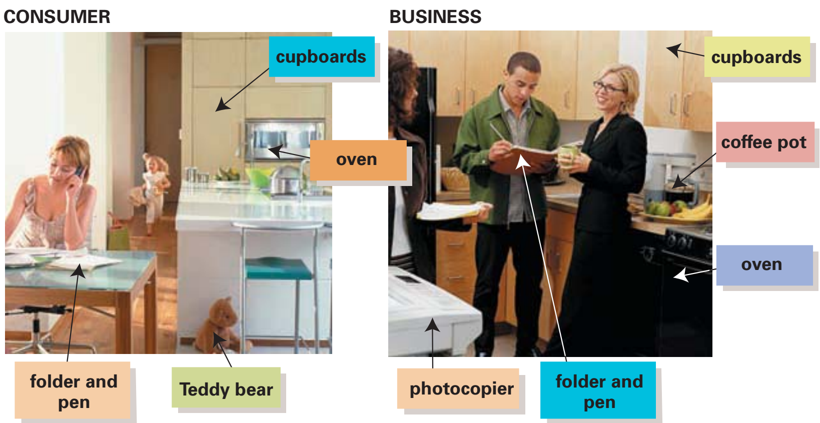
business-to-business electronic commerce
The use of the Internet to facilitate the exchange of goods, services, and information between organizations.

Business marketing is the marketing of goods and services to individuals and organizations for purposes other than personal consumption. The sale of a personal computer to your college or university is an example of business marketing. Business products include those that are used to manufacture other products, become part of another product, or aid the normal operations of an organization. The key characteristic distinguishing business products from consumer products is intended use, not physical characteristics. A product that is purchased for personal or family consumption or as a gift is a consumer good. If that same product, such as a personal computer or a cell phone, is bought for use in a business, it is a business product.

The size of the business market in the United States and most other countries substantially exceeds that of the consumer market. In the business market, a single customer can account for a huge volume of purchases. For example, General Motors' purchasing department spends more than $125 billion per year on goods and services. General Electric, DuPont, and IBM spend over $60 million per day on business purchases.[1]

Review Learning Outcome

LO 1 Describe business marketing



LO 2
Business Marketing on the Internet

The use of the Internet to facilitate activities between organizations is called business-to-business electronic commerce (B-to-B or B2B e-commerce). This method of conducting business has evolved and grown rapidly throughout its short

Marketing & You

Think about the last time you dealt with a salesperson when making a major purchase. Then, using the following scales, indicate your opinions of that salesperson.

Using the scales below, enter your answers.

1	2	3	4	5	6	7
Strongly agree						Strongly disagree

— This salesperson was frank in dealing with me.

— This salesperson did not make false claims.

— I do not think this salesperson was completely open in dealing with me.*

— This salesperson was only concerned about himself/herself.*

— This salesperson did not seem to be concerned with my needs.*

— I did not trust this salesperson.*

— This salesperson was not trustworthy.*

Now, total your score, reversing your answers for the items followed by an asterisk. That is, if you put a 2, change it to a 6; if you put a 3, change it to a 5, and so forth. Read the chapter and find out what your score means at the end.

From Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds. Vol. III, Scale #920. © by American Marketing Association. Used with the permission of the American Marketing Association.

Exhibit 7.1

Internet Sites Specifically for Small Businesses

http://www.allbusiness.com AllBusiness provides entrepreneurs with the knowledge and tools to start, manage, and grow their business. The site links to hundreds of how-to articles and provides expert answers to questions.

http://www.bcentral.com Microsoft bCentral offers small-business solutions such as assistance in establishing an online business presence, enhancing sales or services, or managing business operations. The site also contains practical tips, advice, and links to how-to articles.

http://office.com Office.com offers practical information on how to start or run a business and how to transform an existing company into an e-business. Users access over 500 databases for news that affects their companies or industries. Office.com is one of the ten most visited business Web sites on the Internet.

http://www.quicken.com/small_business/ This site offers information on starting, running, and growing a small business. It also provides links to a variety of other Quicken sites that are useful to small-business owners and managers.

history. In 1995, the commercial Web sites that did exist were static. Only a few had data-retrieval capabilities. Frames, tables, and styles were not available. Security of any sort was rare, and streaming video did not exist. In 2005, there were over one billion Internet users worldwide. In 2008, the United States alone was expected to account for over $1 trillion of B2B e-commerce.[2] Before the Internet, customers had to call Dow Chemical and request a specification sheet for the products they were considering. The information would arrive a few days later by mail. After choosing a product, the customer could then place an order by calling Dow (during business hours, of course). Now, such information is available through **MyAccount@Dow**, which provides information tailored to the customer's requirements. For example, **MyAccount@Dow** offers secure internal monitoring of a customer's chemical tank levels. When tanks reach a predetermined level, reordering can be automatically triggered.[3] This phenomenal growth is not restricted to large companies. Exhibit 7.1 identifies some popular Internet sites that cater to small businesses.

MEASURING ONLINE SUCCESS

To understand what works and what doesn't work online, marketers must be able to comprehend the vast amount of data stored in the log files generated by their Web servers. Not all of these data are relevant for planning an online strategy, but by combining certain log file results with sales information, a marketer can fine-tune the marketing effort to maximize online success.

In the mid-1990s, many Web sites displayed hit counters on their pages. This software device counted the number of file requests made of the server to create the pages seen by visitors. Unfortunately, the hit counters didn't record who visited, how many times they visited, or even what interested the visitors. The counters didn't provide much useful information, and that's why they're rarely seen now.

For marketers today, three of the most important measurements are recency, frequency, and monetary value. *Recency* relates to the fact that customers who have made a purchase recently are more likely to purchase again in the near future than customers who haven't purchased for a while. *Frequency* data help marketers identify frequent purchasers who are definitely more likely to repeat their purchasing behavior in the future. The *monetary value* of sales is important because big spenders can be the most profitable customers for your business.

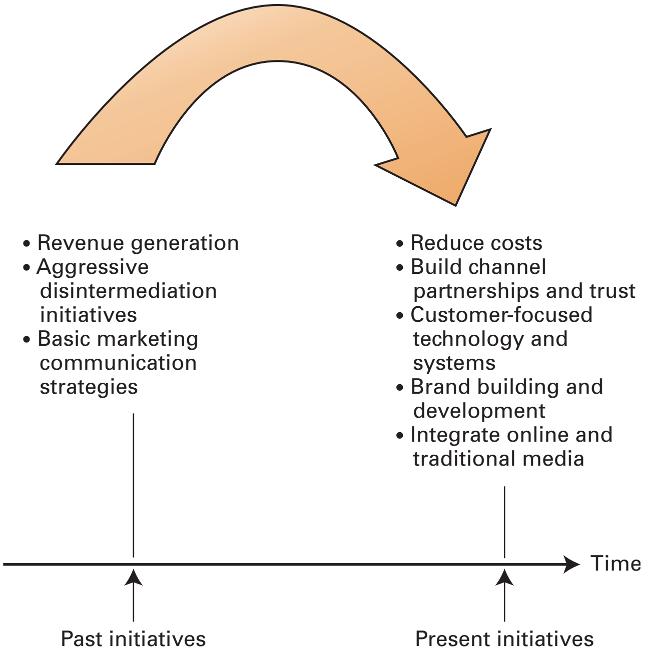
stickiness
A measure of a Web site's effectiveness; calculated by multiplying the frequency of visits times the duration of a visit times the number of pages viewed during each visit (site reach).

NetGenesis, a company that has been purchased by SPSS, devised a number of equations that can help online marketers better understand their data. For example, combining frequency data with the length of time a visitor spent on the Web site (duration) and the number of site pages viewed during each visit (total site reach) can provide an analytical measure of a site's stickiness factor:

$$\text{Stickiness} = \text{Frequency} \times \text{Duration} \times \text{Site Reach}$$

Exhibit 7.2

Evolution of E-Business Initiatives



SOURCE: Andrew J. Rohm and Fareena Sultan, "The Evolution of E-Business," *Marketing Management,* January/February, 2004, p. 35. Used by permission.

By measuring the stickiness factor of a Web site before and after a design or function change, the marketer can quickly determine whether visitors embraced the change. By adding purchase information to determine the level of stickiness needed to provide a desired purchase volume, the marketer gains an even more precise understanding of how a site change affected business. An almost endless number of factor combinations can be created to provide a quantitative method for determining buyer behavior online. First, though, the marketer must determine what measures are required and which factors can be combined to arrive at those measurements.[4]

TRENDS IN B2B INTERNET MARKETING

Over the last decade marketers have become more and more sophisticated in their use of the Internet. Exhibit 7.2 compares three prominent Internet business marketing strategy initiatives from the late 1990s to five that are currently being pursued. Companies have had to transition from "We have a web site because our customer does" to having a store that attracts, interests, satisfies and retains customers. For many companies, e-commerce has become a critical part of their overall marketing strategies.[5] The best online strategy often integrates conventional and Internet marketing strategies. New applications that provide additional information about present and potential customers, increase efficiency, lower costs, increase supply chain efficiency, or enhance customer retention, loyalty, and trust are being developed each year. Chapter 21 on customer relationship management, describes several of these applications.

disintermediation
The elimination of intermediaries such as wholesalers or distributors from a marketing channel.

One term in Exhibit 7.2 that may be unfamiliar is **disintermediation**, which means eliminating intermediaries such as wholesalers or distributors from a marketing channel. A prime example of disintermediation is Dell, Inc., which sells directly to business buyers and consumers. Large retailers such as Wal-Mart use a disintermediation strategy to help reduce costs and prices.[6]

A few years ago, many people thought that the Internet would eliminate the need for distributors. Why would customers pay for distributor markups when they could buy directly from the manufacturers with a few mouse clicks? Yet Internet disintermediation has occurred less frequently than many expected. The reason is that distributors often perform important functions such as providing credit, aggregation of supplies

REVIEW LEARNING OUTCOME

LO 2 Describe the role of the Internet in business marketing

Business Internet Uses

THEN	**Revenue generation** **Aggressive disintermediation initiatives** **Basic marketing communication**
and	
NOW	**Reduce costs** **Build partnerships and alliances** **Build and support branding** **Develop customer-focused technology and systems** **Integrate online and traditional media**

reintermediation
The reintroduction of an intermediary between producers and users.

strategic alliance (strategic partnership)
A cooperative agreement between business firms.

from multiple sources, delivery, and processing returns. Many business customers, especially small firms, depend on knowledgeable distributors for information and advice that aren't available to them online. You will notice in Exhibit 7.2 that building channel partnerships and trust has replaced aggressive disintermediation initiatives as a priority for most firms.

Some firms have followed disintermediation with (reintermediation), the reintroduction of an intermediary between producers and users. They realized that providing direct online purchasing only was similar to having only one store in a city selling a popular brand.[7]

LO3 Relationship Marketing and Strategic Alliances

As Chapter 1 explained, relationship marketing is a strategy that entails seeking and establishing ongoing partnerships with customers. Relationship marketing has become an important business marketing strategy as customers have become more demanding and competition has intensified. Loyal customers are also more profitable than those who are price-sensitive and perceive little or no difference among brands or suppliers. One recent study revealed that the primary marketing goals of U.S. business marketers are customer acquisition, brand awareness, and customer retention, respectively.[8] Building long-term relationships with customers helps companies build competitive advantage that is hard for competitors to copy. For example, the FedEx Powership program includes a series of automated shipping, tracking, and invoicing systems that save customers time and money while solidifying their loyalty to FedEx. This produces a win-win situation. FedEx satisfies a loyal customer, and the customer saves time and money shipping products to its own customers. Similarly, Dell, Inc., provides a customized Web page for each of its premier customers that individual employees in the customer organization can access for information and technical support.

STRATEGIC ALLIANCES

A strategic alliance, sometimes called a *strategic partnership*, is a cooperative agreement between business firms. Strategic alliances can take the form of licensing or distribution agreements, joint ventures, research and development consortia, and partnerships. They may be between different manufacturers, manufacturers and customers, manufacturers and suppliers, and manufacturers and channel intermediaries.

Business marketers form strategic alliances to strengthen operations and better compete. The top executives of Mittal Steel Co., the world's largest steelmaker, have held talks with top officials from South Korean rival, Posco, to assess how they can cooperate by sharing technology and other resources.[9] Sometimes alliance partners' assets are complementary. General Motors Corp. and Shanghai Automotive Industry Corp. have had a partnership for over a decade. GM aids Shanghai Motors by transferring technology and expertise to its Chinese partner. Shanghai, in turn, provides access to the vast Chinese market for automobiles.[10] Experts predict that China will surpass the U.S. as the world's biggest vehicle market by as early as 2010.[11]

Sometimes alliance partners are also fierce competitors. Microsoft Corp. and German software company SAP fit into this category. According to Shai Agassi, chief technology strategist at SAP, "we're both going in with swords drawn, and we're going to do battle until we win... We'll do anything to draw blood."[12] SAP also considers Microsoft its closest partner; the two companies work together to develop joint software and establish industry standards.[13]

Other alliances are formed between companies that operate in completely different industries. Choice Hotels and 1-800-Flowers share call-center employees because doing so is cheaper than outsourcing. When one company experiences increased demand for its products and services, it can call on its partner's employees rather than add staff or use a temporary agency. At a given time, as many as 100 call-center agents may be taking orders for the other company. Both companies report higher employee retention and better recruitment.[14]

relationship commitment
A firm's belief that an ongoing relationship with another firm is so important that the relationship warrants maximum efforts at maintaining it indefinitely.

trust
The condition that exists when one party has confidence in an exchange partner's reliability and integrity.

keiretsu
A network of interlocking corporate affiliates.

For an alliance to succeed in the long term, it must be built on commitment and trust. Relationship commitment means that a firm believes that an ongoing relationship with some other firm is so important that it warrants maximum efforts at maintaining it indefinitely.[15] A perceived reduction in commitment by one of the parties often leads to a breakdown in the relationship.

Trust exists when one party has confidence in an exchange partner's reliability and integrity.[16] Some alliances fail when participants lack trust in their trading partners. General Motors, Ford, Daimler-Chrysler, Nissan Motor Company, and Renault SA created an Internet automobile parts exchange, called Covisint, that was expected to account for $300 billion in sales per year. The auto manufacturers assumed that if they built a Web site, trading volume would follow. But the industry is characterized by mistrust between buyers and sellers. After a decade of being forced to accept price concessions, suppliers were in no hurry to participate. The manufacturers didn't help by boasting that Covisint would squeeze an additional 30 percent in savings out of vendors.

RELATIONSHIPS IN OTHER CULTURES

Although the terms *relationship marketing* and *strategic alliances* are fairly new, and popularized mostly by American business executives and educators, the concepts have long been familiar in other cultures. Businesses in Mexico, China, Japan, Korea, and much of Europe rely heavily on personal relationships. Chapter 21 explores customer relationship management in detail.

In Japan, for example, exchange between firms is based on personal relationships that are developed through what is called *amae*, or indulgent dependency. *Amae* is the feeling of nurturing concern for, and dependence on, another. Reciprocity and personal relationships contribute to *amae*. Relationships between companies can develop into a keiretsu—a network of interlocking corporate affiliates. Within a keiretsu, executives may sit on the boards of their customers or their suppliers. Members of a keiretsu trade with each other whenever possible and often engage in joint product development, finance, and marketing activity. For example, the Toyota Group keiretsu includes 14 core companies and another 170 that receive preferential treatment. Toyota holds an equity position in many of these 170 member firms and is represented on many of their boards of directors.

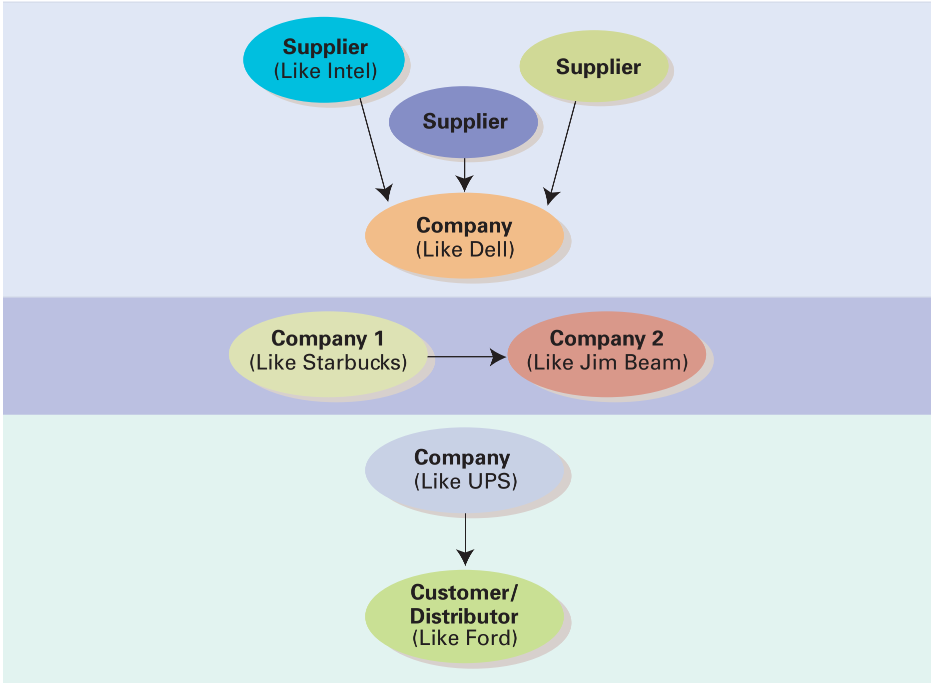
Many American firms have found that the best way to compete in Asian countries is to form relationships with Asian firms. For example, General Motors joint venture with Shanghai Motors produces Buicks, Chevrolets and Cadillacs. German automaker Volkswagen also has an alliance with Shanghai Motors to produce the Passat.[17]

© AP PHOTO/GREG BAKER/GM CHINA

General Motors, Tsinghua University in China, and Shanghai Automotive Industries Corp., have a product development relationship. GM recently set up a multi-million-dollar alternative fuel research center in Shanghai, and funded "The China Automotive Energy Research Center."

REVIEW LEARNING OUTCOME

LO3 Discuss the role of relationship marketing and strategic alliances in business marketing



LO4

Major Categories of Business Customers

The business market consists of four major categories of customers: producers, resellers, governments, and institutions.

PRODUCERS

The producer segment of the business market includes profit-oriented individuals and organizations that use purchased goods and services to produce other products, to incorporate into other products, or to facilitate the daily operations of the organization. Examples of producers include construction, manufacturing, transportation, finance, real estate, and food service firms. In the United States there are over 13 million firms in the producer segment of the business market. Some of these firms are small, and others are among the world's largest businesses.

Producers are often called original equipment manufacturers or OEMs. This term includes all individuals and organizations that buy business goods and incorporate them into the products that they produce for eventual sale to other producers or to consumers. Companies such as General Motors that buy steel, paint, tires, and batteries are said to be OEMs.

original equipment manufacturers (OEMs) Individuals and organizations that buy business goods and incorporate them into the products that they produce for eventual sale to other producers or to consumers.

RESELLERS

The reseller market includes retail and wholesale businesses that buy finished goods and resell them for a profit. A retailer sells mainly to final consumers; wholesalers sell mostly to retailers and other organizational customers. There are approximately 1.5 million retailers and 500,000 wholesalers operating in the United States. Consumer-product firms like Procter & Gamble, Kraft Foods, and Coca-Cola sell directly to large retailers and retail chains and through wholesalers to smaller retail units. Retailing is explored in detail in Chapter 15.

Business product distributors are wholesalers that buy business products and resell them to business customers. They often carry thousands of items in stock and employ sales forces to call on business customers. Businesses that wish to buy a gross of pencils or a hundred pounds of fertilizer typically purchase these items from local distributors rather than directly from manufacturers such as Empire Pencil or Dow Chemical.

GOVERNMENTS

A third major segment of the business market is government. Government organizations include thousands of federal, state, and local buying units. They make up what may be the largest single market for goods and services in the world.

Contracts for government purchases are often put out for bid. Interested vendors submit bids (usually sealed) to provide specified products during a particular time. Sometimes the lowest bidder is awarded the contract. When the lowest bidder is not awarded the contract, strong evidence must be presented to justify the decision. Grounds for rejecting the lowest bid include lack of experience, inadequate financing, or poor past performance. Bidding allows all potential suppliers a fair chance at winning government contracts and helps ensure that public funds are spent wisely.

Federal Government

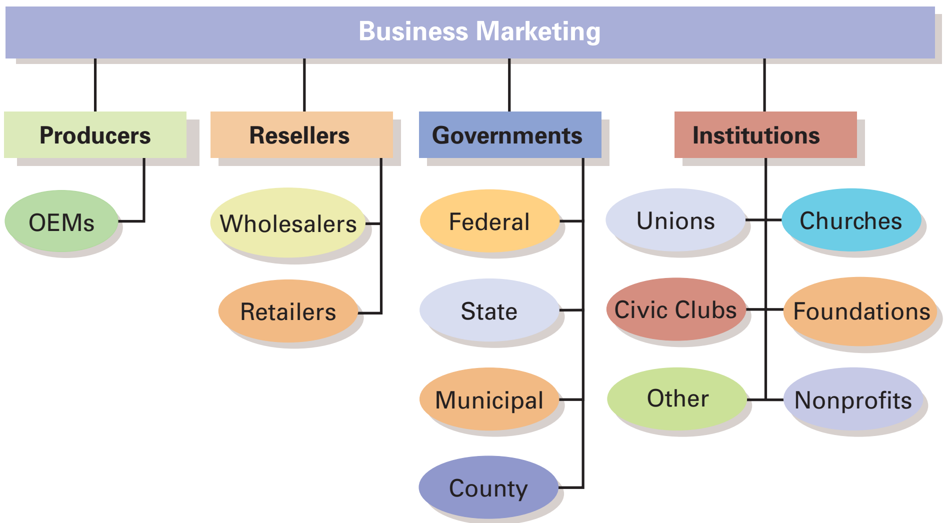
Name just about any good or service and chances are that someone in the federal government uses it. The U.S. federal government buys goods and services valued at over $600 billion per year, making it the world's largest customer.

Although much of the federal government's buying is centralized, no single federal agency contracts for all the government's requirements, and no single buyer in any agency purchases all that the agency needs. We can view the federal government as a combination of several large companies with overlapping responsibilities and thousands of small independent units.

One popular source of information about government procurement is *Commerce Business Daily*. Until recently, businesses hoping to sell to the federal government found the document unorganized, and it often arrived too late to be useful. The online version (**http:// www.cbd-net.com**) is more timely and lets contractors find leads using keyword searches. *Doing Business with the General Services Administration*, *Selling to the Military*, and *Selling to the U.S. Air Force* are other examples of publications designed to explain how to do business with the federal government.

REVIEW LEARNING OUTCOME

LO4 Identify the four major categories of business market customers



State, County, and City Government

For both large and small vendors, selling to states, counties, and cities can be less frustrating than selling to the federal government. Paperwork is typically simpler and more manageable than it is at the federal level. On the other hand, vendors must decide which of the over 82,000 government units are likely to buy their wares. State and local buying agencies include school districts, highway departments, government-operated hospitals, and housing agencies.

INSTITUTIONS

North American Industry Classification System (NAICS) A detailed numbering system developed by the United States, Canada, and Mexico to classify North American business establishments by their main production processes.

The fourth major segment of the business market consists of institutions that seek to achieve goals other than the standard business goals of profit, market share, and return on investment. This segment includes schools, hospitals, colleges and universities, churches, labor unions, fraternal organizations, civic clubs, foundations, and other so-called nonbusiness organizations. Xerox offers educational and medical institutions the same prices as government agencies (the lowest that Xerox offers) and has a separate sales force that calls on these customers.

LO5

The North American Industry Classification System

The North American Industry Classification System (NAICS) is an industry classification system introduced in 1997 to replace the standard industrial classification system (SIC). NAICS (pronounced *nakes*) is a system for classifying North American business establishments. The system, developed jointly by the United States, Canada, and Mexico, provides a common industry classification system for the North American Free Trade Agreement (NAFTA) partners. Goods- or service-producing firms that use identical or similar production processes are grouped together.

NAICS is an extremely valuable tool for business marketers engaged in analyzing, segmenting, and targeting markets. Each classification group is relatively homogeneous in terms of raw materials required, components used, manufacturing processes employed, and problems faced. The more digits in a code, the more homogeneous the group is. Therefore, if a supplier understands the needs and requirements of a few firms within a classification, requirements can be projected for all firms in that category. The number, size, and geographic dispersion of firms can also be identified. This information can be converted to market potential estimates, market share estimates, and sales forecasts. It can also be used for identifying potential new customers. NAICS codes can help identify firms that may be prospective users of a supplier's goods and services.

Exhibit 7.3 provides an overview of NAICS. Exhibit 7.4 illustrates the six-digit classification system for two of the 20 NAICS economic sectors: manufacturing and information. The hierarchical structure of NAICS allows industry data to be summarized at several levels of detail. To illustrate:

- The first two digits designate a major economic sector such as agriculture (11) or manufacturing (31–33).

Exhibit 7.3

NAICS Two-Digit Codes and Corresponding Economic Sectors

NAICS Code	Economic Sector
11	Agriculture, forestry, and fishing
21	Mining
22	Utilities
23	Construction
31–33	Manufacturing
43	Wholesale trade
44–45	Retail trade
47–48	Transportation
51	Information
52	Finance and insurance
53	Real estate and rental and leasing
56	Professional and technical services
57	Management and support services
61	Education services
62	Health and social assistance
71	Arts, entertainment, and recreation
72	Food services, drinking places, and accommodations
81	Other services, except public administration
93	Public administration
98	Estates and trusts
99	Nonclassifiable

Exhibit 7.4

Examples of NAICS Hierarchy

	Example 1		Example 2	
NAICS Level	**NAICS Code**	**Description**	**NAICS Code**	**Description**
Sector	31–33	Manufacturing	51	Information
Subsector	334	Computer and electronic product manufacturing	513	Broadcasting and telecommunications
Industry group	3346	Manufacturing and reproduction of magnetic and optical media	5133	Telecommunications
Industry	33461	Manufacturing and reproduction of magnetic and optical media	51332	Wireless telecommunications carriers, except satellite
Industry Subdivision	334611	Reproduction of software	513321	Paging

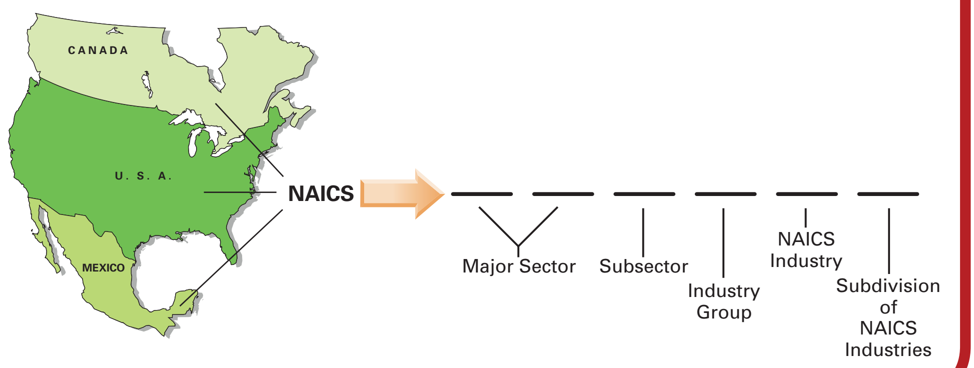
SOURCE: U.S. Census Bureau, "New Code System In NAICS," **http://www.census.gov/epcd/www/naics.html.**

- The third digit designates an economic subsector such as crop production or apparel manufacturing.
- The fourth digit designates an industry group, such as grain and oil seed farming or fiber, yarn, and thread mills.
- The fifth digit designates the NAICS industry, such as wheat farming or broadwoven fabric mills.
- The sixth digit, when used, identifies subdivisions of NAICS industries that accommodate user needs in individual countries.[18]

For a complete listing of all NAICS codes, see **http://www.censusgov/epcd/www/naics.html**.

REVIEW LEARNING OUTCOME

LO5 Explain the North American Industry Classification System



LO6

Business versus Consumer Markets

The basic philosophy and practice of marketing are the same

whether the customer is a business organization or a consumer. Business markets do, however, have characteristics different from consumer markets.

DEMAND

Consumer demand for products is quite different from demand in the business market. Unlike consumer demand, business demand is derived, inelastic, joint, and fluctuating.

derived demand
The demand for business products.

joint demand
The demand for two or more items used together in a final product.

multiplier effect (accelerator principle)
Phenomenon in which a small increase or decrease in consumer demand can produce a much larger change in demand for the facilities and equipment needed to make the consumer product.

Derived Demand

The demand for business products is called derived demand because organizations buy products to be used in producing their customers' products. For example, the market for CPUs, hard drives, and CD-ROMs is derived from the demand for personal computers. These items are only valuable as components of computers. Demand for these items rises and falls with the demand for PCs.

Because demand is derived, business marketers must carefully monitor demand patterns and changing preferences in final consumer markets, even though their customers are not in those markets. Moreover, business marketers must carefully monitor their customers' forecasts, because derived demand is based on expectations of future demand for those customers' products.

Some business marketers not only monitor final consumer demand and customer forecasts but also try to influence final consumer demand. Aluminum producers use television and magazine advertisements to point out the convenience and recycling opportunities that aluminum offers to consumers who can choose to purchase soft drinks in either aluminum or plastic containers.

Inelastic Demand

The demand for many business products is inelastic with regard to price. *Inelastic demand* means that an increase or decrease in the price of the product will not significantly affect demand for the product. This will be discussed further in Chapter 19.

The price of a product used in the production of, or as part of, a final product is often a minor portion of the final product's total price. Therefore, demand for the final consumer product is not affected. If the price of automobile paint or spark plugs rises significantly, say, 200 percent in one year, do you think the number of new automobiles sold that year will be affected? Probably not.

Joint Demand

Joint demand occurs when two or more items are used together in a final product. For example, a decline in the availability of memory chips will slow production of microcomputers, which will in turn reduce the demand for disk drives. Likewise, the demand for Apple operating systems exists as long as there is demand for Apple computers. Sales of the two products are directly linked.

Fluctuating Demand

The demand for business products—particularly new plants and equipment—tends to be less stable than the demand for consumer products. A small increase or decrease in consumer demand can produce a much larger change in demand for the facilities and equipment needed to make the consumer product. Economists refer to this phenomenon as the multiplier effect (or accelerator principle).

Cummins Engine Company, a producer of heavy-duty diesel engines, uses sophisticated surface grinders to make parts. Suppose Cummins is using 20 surface grinders. Each machine lasts about 10 years. Purchases have been timed so two machines will wear out and be replaced annually. If the demand for engine parts does not change, two grinders will be bought this year. If the demand for parts declines slightly, only 18 grinders may be needed and Cummins won't replace the worn ones. However, suppose that next year demand returns to previous levels plus a little more. To meet the new level of demand, Cummins will need to replace the two machines that wore out in the first year, the two that wore out in the second year, plus one or more additional machines. The multiplier effect works this way in many industries, producing highly fluctuating demand for business products.

PURCHASE VOLUME

Business customers buy in much larger quantities than consumers. Just think how large an order Kellogg typically places for the wheat bran and raisins used to manufacture Raisin Bran. Imagine the number of tires that Chrysler buys at one time.

NUMBER OF CUSTOMERS

Business marketers usually have far fewer customers than consumer marketers. The advantage is that it is a lot easier to identify prospective buyers, monitor current customers' needs and levels of satisfaction, and personally attend to existing customers. The main disadvantage is that each customer becomes crucial—especially for those manufacturers that have only one customer. In many cases, this customer is the U.S. government. The success or failure of one bid can make the difference between prosperity and bankruptcy. After five years of development, testing, and politicking, the Pentagon awarded Lockheed Martin a multidecade contract to build 3,000 jet fighter airplanes. Boeing Aircraft Company, the only other bidder on the $200 billion contract, immediately announced plans for substantial layoffs.

LOCATION OF BUYERS

business-to-business online exchange
An electronic trading floor that provides companies with integrated links to their customers and suppliers.

Business customers tend to be much more geographically concentrated than consumers. For instance, more than half the nation's business buyers are located in New York, California, Pennsylvania, Illinois, Ohio, Michigan, and New Jersey. The aircraft and microelectronics industries are concentrated on the West Coast, and many of the firms that supply the automobile manufacturing industry are located in and around Detroit. Companies that make orthopedic devices are even concentrated, with three of the world's five largest makers of artificial joints and related tools headquartered in tiny Warsaw, Indiana.[19] A total of 28 orthopedic companies employing 6,500 people are located within a seven-mile radius.[20]

DISTRIBUTION STRUCTURE

Many consumer products pass through a distribution system that includes the producer, one or more wholesalers, and a retailer. In business marketing, however, because of many of the characteristics already mentioned, channels of distribution are typically shorter. Direct channels, where manufacturers market directly to users, are much more common. The use of direct channels has increased dramatically in the past decade with the introduction of various Internet buying and selling schemes. One such technique is a business-to-business online exchange, is an electronic trading floor that provides companies with integrated links to their customers and suppliers. The goal of a B2B online exchange is to simplify business purchasing and make it more efficient. For example, Exostar, the aerospace industry's online exchange, has over 12,000 participating suppliers and conducts more than 20,000 transactions each week.[21] Exchanges such as Exostar facilitate direct channel relationships between producers and their customers.

NATURE OF BUYING

Unlike consumers, business buyers usually approach purchasing rather formally. Businesses use professionally trained purchasing agents or buyers who spend their entire career purchasing a limited number of items. They get to know the items and the sellers well. Some professional purchasers earn the designation of Certified Purchasing Manager (CPM) after participating in a rigorous certification program.

NATURE OF BUYING INFLUENCE

Typically, more people are involved in a single business purchase decision than in a consumer purchase. Experts from fields as varied as quality control, marketing, and finance, as well as professional buyers and users, may be grouped in a buying center (discussed later in this chapter).

TYPE OF NEGOTIATIONS

Consumers are used to negotiating price on automobiles and real estate. In most cases, however, American consumers expect sellers to set the price and other conditions of sale, such as time of delivery and credit terms. In contrast, negotiating is common in business marketing. Buyers and sellers negotiate product specifications, delivery dates, payment terms, and other pricing matters. Sometimes these negotiations occur during many meetings over several months. Final contracts are often very long and detailed.

USE OF RECIPROCITY

reciprocity
The practice of business purchasers choosing to buy from their own customers.

Business purchasers often choose to buy from their own customers, a practice known as reciprocity. For example, General Motors buys engines for use in its automobiles and trucks from Borg Warner, which in turn buys many of the automobiles and trucks it needs from GM. This practice is neither unethical nor illegal unless one party coerces the other, creating unfair competition. Reciprocity is generally considered a reasonable business practice. If all possible suppliers sell a similar product for about the same price, doesn't it make sense to buy from those firms that buy from you?

REVIEW LEARNING OUTCOME

LO 6 Explain the major differences between business and consumer markets

Characteristic	Business Market	Consumer Market
Demand	Organizational	Individual
Purchase volume	Larger	Smaller
Number of customers	Fewer	Many
Location of buyers	Geographically concentrated	Dispersed
Distribution structure	More direct	More indirect
Nature of buying	More professional	More personal
Nature of buying influence	Multiple	Single
Type of negotiations	More complex	Simpler
Use of reciprocity	Yes	No
Use of leasing	Greater	Lesser
Primary promotional method	Personal selling	Advertising

USE OF LEASING

Consumers normally buy products rather than lease them. But businesses commonly lease expensive equipment such as computers, construction equipment and vehicles, and automobiles. Leasing allows firms to reduce capital outflow, acquire a seller's latest products, receive better services, and gain tax advantages.

The lessor, the firm providing the product, may be either the manufacturer or an independent firm. The benefits to the lessor include greater total revenue from leasing compared to selling and an opportunity to do business with customers who cannot afford to buy.

PRIMARY PROMOTIONAL METHOD

Business marketers tend to emphasize personal selling in their promotion efforts, especially for expensive items, custom-designed products, large-volume purchases, and situations requiring negotiations. The sale of many business products requires a great deal of personal contact. Personal selling is discussed in more detail in Chapter 18.

LO7

Types of Business Products

Business products generally fall into one of the following seven categories, depending on their use: major equipment, accessory equipment, raw materials, component parts, processed materials, supplies, and business services.

MAJOR EQUIPMENT

major equipment (installations)
Capital goods such as large or expensive machines, mainframe computers, blast furnaces, generators, airplanes, and buildings.

accessory equipment
Goods, such as portable tools and office equipment, that are less expensive and shorter-lived than major equipment.

raw materials
Unprocessed extractive or agricultural products, such as mineral ore, timber, wheat, corn, fruits, vegetables, and fish.

Major equipment includes such capital goods as large or expensive machines, mainframe computers, blast furnaces, generators, airplanes, and buildings. (These items are also commonly called installations.) Major equipment is depreciated over time rather than charged as an expense in the year it is purchased. In addition, major equipment is often custom-designed for each customer. Personal selling is an important part of the marketing strategy for major equipment because distribution channels are almost always direct from the producer to the business user.

ACCESSORY EQUIPMENT

Accessory equipment is generally less expensive and shorter-lived than major equipment. Examples include portable drills, power tools, microcomputers, and fax machines. Accessory equipment is often charged as an expense in the year it is bought rather than depreciated over its useful life. In contrast to major equipment, accessories are more often standardized and are usually bought by more customers. These customers tend to be widely dispersed. For example, all types of businesses buy microcomputers.

Local industrial distributors (wholesalers) play an important role in the marketing of accessory equipment because business buyers often purchase accessories from them. Regardless of where accessories are bought, advertising is a more vital promotional tool for accessory equipment than for major equipment.

RAW MATERIALS

Raw materials are unprocessed extractive or agricultural products—for example, mineral ore, timber, wheat, corn, fruits, vegetables, and fish. Raw materials become part of finished products. Extensive users, such as steel or lumber mills and food canners, generally buy huge quantities of raw materials. Because there is often a large number of relatively small sellers of raw materials, none can greatly influence price or supply. Thus, the market tends to set the price of raw materials, and individual producers have little pricing flexibility. Promotion is almost always via personal selling, and distribution channels are usually direct from producer to business user.

COMPONENT PARTS

component parts
Either finished items ready for assembly or products that need very little processing before becoming part of some other product.

processed materials
Products used directly in manufacturing other products.

supplies
Consumable items that do not become part of the final product.

Component parts are either finished items ready for assembly or products that need very little processing before becoming part of some other product. Caterpillar diesel engines are component parts used in heavy-duty trucks. Other examples include spark plugs, tires, and electric motors for automobiles. A special feature of component parts is that they can retain their identity after becoming part of the final product. For example, automobile tires are clearly recognizable as part of a car. Moreover, because component parts often wear out, they may need to be replaced several times during the life of the final product. Thus, there are two important markets for many component parts: the original equipment manufacturer (OEM) market and the replacement market.

Many of the business features listed in the review for Learning Outcome 6 characterize the OEM market. The difference between unit costs and selling prices in the OEM market is often small, but profits can be substantial because of volume buying.

The replacement market is composed of organizations and individuals buying component parts to replace worn-out parts. Because components often retain their identity in final products, users may choose to replace a component part with the same brand used by the manufacturer—for example, the same brand of automobile tires or battery. The replacement market operates differently from the OEM market, however. Whether replacement buyers are organizations or individuals, they tend to demonstrate the characteristics of consumer markets that were shown in the review for Learning Outcome 6. Consider, for example, an automobile replacement part. Purchase volume is usually small and there are many customers, geographically dispersed, who typically buy from car dealers or parts stores. Negotiations do not occur, and neither reciprocity nor leasing is usually an issue.

Manufacturers of component parts often direct their advertising toward replacement buyers. Cooper Tire & Rubber, for example, makes and markets component parts—automobile and truck tires—for the replacement market only. General Motors and other car makers compete with independent firms in the market for replacement automobile parts.

Even though the Internet has greatly affected the consumption of many supplies, like envelopes, paper is still in high demand. In fact, computer technology has increased the demand for paper rather than squelching it.

PROCESSED MATERIALS

Processed materials are products used directly in manufacturing other products. Unlike raw materials, they have had some processing. Examples include sheet metal, chemicals, specialty steel, lumber, corn syrup, and plastics. Unlike component parts, processed materials do not retain their identity in final products.

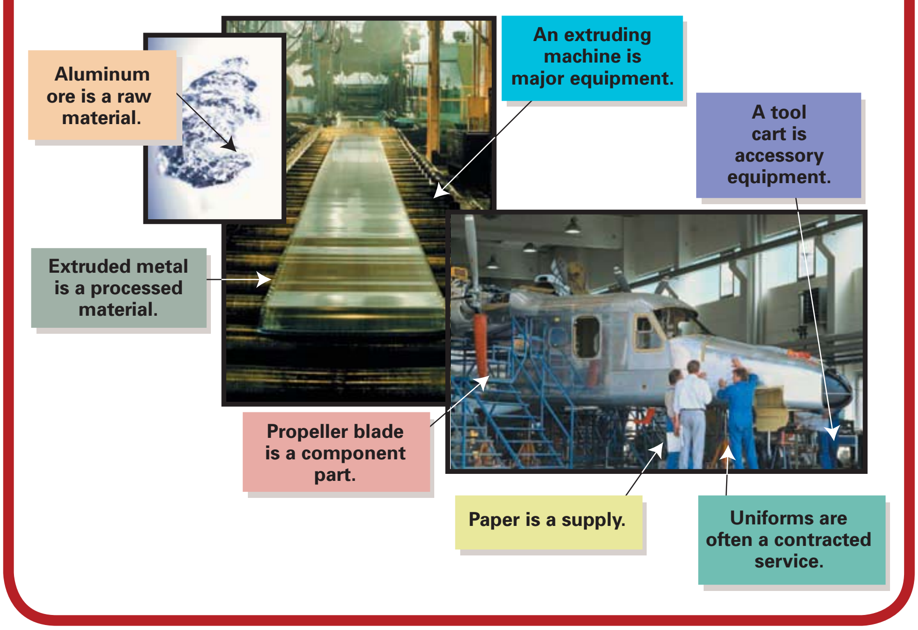
Most processed materials are marketed to OEMs or to distributors servicing the OEM market. Processed materials are generally bought according to customer specifications or to some industry standard, as is the case with steel and plywood. Price and service are important factors in choosing a vendor.

SUPPLIES

Supplies are consumable items that do not become part of the final product—for example, lubricants, detergents, paper towels, pencils, and paper. Supplies are normally standardized items that purchasing agents routinely buy. Supplies typically have relatively short lives and are inexpensive compared to other business goods. Because supplies generally fall into one of three categories—maintenance,

REVIEW LEARNING OUTCOME

LO7 Describe the seven types of business goods and services



repair, or operating supplies—this category is often referred to as MRO items.

Competition in the MRO market is intense. Bic and Paper Mate, for example, battle for business purchases of inexpensive ballpoint pens.

BUSINESS SERVICES

Business services are expense items that do not become part of a final product. Businesses often retain outside providers to perform janitorial, advertising, legal, management consulting, marketing research, maintenance, and other services. Hiring an outside provider makes sense when it costs less than hiring or assigning an employee to perform the task and when an outside provider is needed for particular expertise.

LO8 Business Buying Behavior

business services
Expense items that do not become part of a final product.

buying center
All those persons in an organization who become involved in the purchase decision.

As you've probably already concluded, business buyers behave differently from consumers. Understanding how purchase decisions are made in organizations is a first step in developing a business selling strategy. Business buying behavior has five important aspects: buying centers, evaluative criteria, buying situations, business ethics, and customer service.

BUYING CENTERS

In many cases, more than one person is involved in a purchase decision. Identifying who these people are and the roles that they play greatly enhances the salesperson's chances for success.[22]

A **buying center** includes all those persons in an organization who become involved in the purchase decision. Membership and influence vary from company to company. For instance, in engineering-dominated firms like Bell Helicopter, the buying center may consist almost entirely of engineers. In marketing-oriented firms like Toyota and IBM, marketing and engineering have almost equal authority. In consumer goods firms like Procter & Gamble, product managers and other marketing decision makers may dominate the buying center. In a small manufacturing company, almost everyone may be a member.

The number of people involved in a buying center varies with the complexity and importance of a purchase decision. The composition of the buying group will usually change from one purchase to another and sometimes even during various stages of the buying process. To make matters more complicated, buying centers do not appear on formal organizational charts.

For example, even though a formal committee may have been set up to choose a new plant site, it is only part of the buying center. Other people, like the company president, often play informal yet powerful roles. In a lengthy decision-making process, such as finding a new plant location, some members may drop out of the

Exhibit 7.5

Buying-Center Roles for Computer Purchases

Role	Illustration
Initiator	Division general manager proposes to replace company's computer network.
Influencers/ evaluators	Corporate controller's office and vice president of data processing have an important say in which system and vendor the company will deal with.
Gatekeepers	Corporate departments for purchasing and data processing analyze company's needs and recommend likely matches with potential vendors.
Decider	Vice president of administration, with advice from others, selects vendor the company will deal with and system it will buy.
Purchaser	Purchasing agent negotiates terms of sale.
Users	All division employees use the computers.

buying center when they can no longer play a useful role. Others whose talents are needed then join the center. Buying centers never formally announce "who is in" and "who is out".

Roles in the Buying Center

As in family purchasing decisions, several people may play a role in the business purchase process:

- *Initiator:* the person who first suggests making a purchase.
- *Influencers/evaluators:* people who influence the buying decision. They often help define specifications and provide information for evaluating options. Technical personnel are especially important as influencers.
- *Gatekeepers:* group members who regulate the flow of information. Frequently, the purchasing agent views the gatekeeping role as a source of his or her power. A secretary may also act as a gatekeeper by determining which vendors get an appointment with a buyer.
- *Decider:* the person who has the formal or informal power to choose or approve the selection of the supplier or brand. In complex situations, it is often difficult to determine who makes the final decision.
- *Purchaser:* the person who actually negotiates the purchase. It could be anyone from the president of the company to the purchasing agent, depending on the importance of the decision.
- *Users:* members of the organization who will actually use the product. Users often initiate the buying process and help define product specifications.

Exhibit 7.7 illustrates these basic roles.

Implications of Buying Centers for the Marketing Manager

Successful vendors realize the importance of identifying who is in the decision-making unit, each member's relative influence in the buying decision, and each member's evaluative criteria. Successful selling strategies often focus on determining the most important buying influences and tailoring sales presentations to the evaluative criteria most important to these buying-center members.

For example, Loctite Corporation, the manufacturer of Super Glue and industrial adhesives and sealants, found that engineers were the most important influencers and deciders in adhesive and sealant purchase decisions. As a result, Loctite focused its marketing efforts on production and maintenance engineers.

EVALUATIVE CRITERIA

Business buyers evaluate products and suppliers against three important criteria: quality, service, and price—in that order.

Quality

In this case, quality refers to technical suitability. A superior tool can do a better job in the production process, and superior packaging can increase dealer and consumer acceptance of a brand. Evaluation of quality also applies to the salesperson and the salesperson's firm. Business buyers want to deal with reputable salespeople and financially responsible companies. Quality improvement should be part of every organization's marketing strategy.

Service

Almost as much as they want satisfactory products, business buyers want satisfactory service. A purchase offers several opportunities for service. Suppose a vendor is selling heavy equipment. Prepurchase service could include a survey of the buyer's needs. After thorough analysis of the survey findings, the vendor could prepare a report and recommendations in the form of a purchasing proposal. If a purchase results, postpurchase service might consist of installing the equipment and training those who will be using it. Postsale services may also include maintenance and repairs. Another service that business buyers seek is supply dependability. They must be able to count on getting what they ordered delivered on schedule. Buyers also welcome services that help them sell their finished products, especially when the seller's product is an identifiable part of the buyer's end product.

Price

Business buyers want to buy at low prices—at the lowest prices, under most circumstances. However, a buyer who pressures a supplier to cut prices to a point where the supplier loses money on the sale often forces shortcuts on quality. The buyer may also, in effect, force the supplier to quit selling to him or her. Then he or she will have to find a new supply source.

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A manufacturer, such as Briggs & Stratton Corporation, must sometimes decide whether to make something or buy it from an outside supplier. For example, should the company spend $500,000 to buy new equipment to make gas throttles or spend the same amount to upgrade its carburetor assembly line? It must determine which "buy" is the best use of company resources.

BUYING SITUATIONS

Often business firms, especially manufacturers, must decide whether to make something or buy it from an outside supplier. The decision is essentially one of economics. Can an item of similar quality be bought at a lower price elsewhere? If not, is manufacturing it in-house the best use of limited company resources? For example, Briggs & Stratton Corporation, a major manufacturer of four-cycle engines, might be able to save $150,000 annually on outside purchases by spending $500,000 on the equipment needed to produce gas throttles internally. Yet Briggs & Stratton could also use that $500,000 to upgrade its carburetor assembly line, which would save $225,000 annually. Assuming a firm decides to buy a product instead of making it, the purchase will be a new buy, a modified rebuy, or a straight rebuy.

New Buy

A new buy is a situation requiring the purchase of a product for the first time. For example, suppose a manufacturing company needs a better way to page managers while they are working on the shop floor. Currently, each of the several managers has a distinct ring, for example, two short and one long, that sounds over the plant intercom whenever he or she is being paged by anyone in the factory. The company decides to replace its buzzer system of paging with handheld wireless radio technology that will enable managers to communicate immediately with the department initiating the page. This situation represents the greatest opportunity for new vendors. No long-term relationship has been established for this product, specifications may be somewhat fluid, and buyers are generally open to new vendors.

If the new item is a raw material or a critical component part, the buyer cannot afford to run out of supply. The seller must convince the buyer that the seller's firm can consistently deliver a high-quality product on time.

new buy
A situation requiring the purchase of a product for the first time.

modified rebuy
A situation where the purchaser wants some change in the original good or service.

straight rebuy
A situation in which the purchaser reorders the same goods or services without looking for new information or investigating other suppliers.

Modified Rebuy

A modified rebuy is normally less critical and less time-consuming than a new buy. In a modified-rebuy situation, the purchaser wants some change in the original good or service. It may be a new color, greater tensile strength in a component part, more respondents in a marketing research study, or additional services in a janitorial contract.

Because the two parties are familiar with each other and credibility has been established, buyer and seller can concentrate on the specifics of the modification. But in some cases, modified rebuys are open to outside bidders. The purchaser uses this strategy to ensure that the new terms are competitive. An example would be the manufacturing company buying radios with a vibrating feature for managers who have trouble hearing the ring over the factory noise. The firm may open the bidding to examine the price/quality offerings of several suppliers.

Straight Rebuy

A straight rebuy is a situation vendors prefer. The purchaser is not looking for new information or other suppliers. An order is placed and the product is provided as in previous orders. Usually, a straight rebuy is routine because the terms of the purchase have been agreed to in earlier negotiations. For example, if our manufacturing company purchases additional radios for new managers from the same supplier on a regular basis.

One common instrument used in straight-rebuy situations is the purchasing contract. Purchasing contracts are used with products that are bought frequently and in high volume. In essence, the purchasing contract makes the buyer's decision making routine and promises the salesperson a sure sale. The advantage to the buyer is a quick, confident decision and to the salesperson, reduced or eliminated competition.

Suppliers must remember not to take straight-rebuy relationships for granted. Retaining existing customers is much easier than attracting new ones.

BUSINESS ETHICS

As we noted in Chapter 3, ethics refers to the moral principles or values that generally govern the conduct of an individual or a group. Ethics can also be viewed as the standard of behavior by which conduct is judged.

Although we have heard about lots of corporate misbehavior in recent years, most people, and most companies, follow ethical practices. To help achieve this, over half of all major corporations offer ethics training to employees. Many companies also have codes of ethics or business conduct to guide buyers and sellers. The "Ethics in Marketing" box shows Texas Instruments Incorporated's Code of Business Conduct.

CUSTOMER SERVICE

Business marketers are increasingly recognizing the benefits of developing a formal system to monitor customer opinions and perceptions of customer service quality. Companies like McDonald's, L.L. Bean, and Lexus build their strategies not only around products, but also around a few highly developed service skills. These companies understand that keeping current customers satisfied is just as important as attracting new ones, if not more so. These leading-edge firms are obsessed not only with delivering high-quality customer service, but also with measuring satisfaction, loyalty, relationship quality, and other indicators of nonfinancial performance.

Most firms find it necessary to develop measures unique to their own strategy, value propositions, and target market. For example, Anderson Corporation assesses the loyalty of its trade customers by their willingness to continue carrying its windows and doors, recommending its products to colleagues and customers, increasing their volume with the company, and installing its products in their own homes. Basically, each firm's measures should not only ask "what are your expectations?" and "how are we doing?" but should also reflect what the firm wants its customers to do.

Some customers are more valuable than others. They may have greater value because they spend more, buy higher-margin products, have a well-known name, or might potentially become a bigger customer in the future. Some companies selectively provide different levels of service to customers based on their value to the business. By giving the most valuable customers superior service, a firm is more likely to keep them happy, hopefully increasing retention of these high-value customers and maximizing

ETHICS in Marketing

Texas Instruments Inc. (TI): Values and Ethics Statement and Code of Business Conduct

ETHICS

The Code of Business Conduct contains principles that have long been part of Texas Instruments' values and ethics statements. Certain behaviors have been specifically included in this Code of Business Conduct in recognition of the growing interest that investors have in the conduct of publicly-held companies, their employees and their directors. The public has every right to know what TI standards are in these areas. Furthermore, the public legitimately expects TIers to know and adhere to the standards of conduct. This Code of Business Conduct is intended to comply with New York Stock Exchange listing standards. Employees should refer to the section below entitled Compliance Procedures, Policies and Rules for guidance on complying with this Code of Business Conduct. No provision of this Code of Business Conduct may be waived for any director or executive officer without approval of the TI Board of Directors, and appropriate public disclosure.

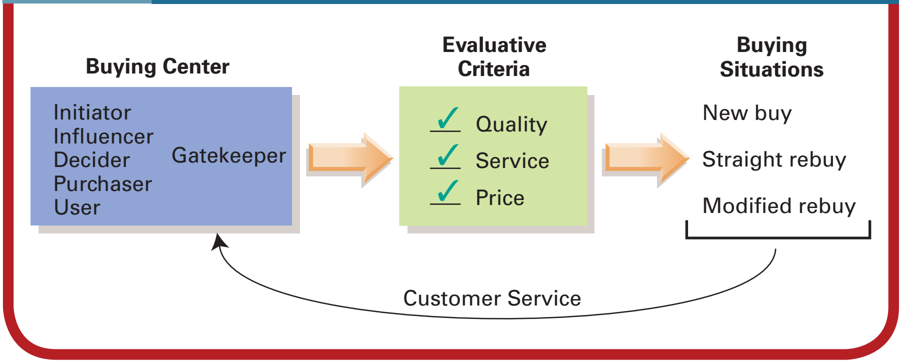
- We do not take any role in any outside concern that would adversely influence our TI responsibilities. When faced with a potential conflict, we communicate with supervisors and others to implement safeguard and take steps to prevent such a conflict from materializing. We make full disclosure and withdraw ourselves from discussions and decisions when our personal interest appears to interfere with TI's business interests.
- When exchanging business courtesies, meals and entertainment, we avoid activities that could create even the appearance that our decisions could be compromised.
- We respect the right and property of others, including their intellectual property, and only accept their confidential or trade secret information after we clearly understand our obligations as defined in a non-disclosure agreement or similar document. We protect and preserve TI assets, including TI business opportunities and intellectual property, for TI's benefit and not for our personal benefit.
- We compete fairly without collusion or collaboration with competitors to divide markets, fix prices, restrict production or allocate customers.
- We assure that those who seek to do business with TI have fair opportunities to compete for our business.
- We provide full and accurate information for use in internal and external reports.
- We keep records that are verifiably accurate.
- We use company assets for personal purposes strictly on an infrequent basis with negligible expense to TI.
- We recruit, train, promote and reward people based on their performance and contribution.
- We respect all TIers without regard to their position or level within the organization.
- We follow the Code of Business Conduct and respect the codes of conduct, and rules of business of countries where we do business, and abide by their laws.
- We comply with laws, rules and regulations, and actively promote awareness and understanding of, and compliance with all applicable laws.
- We promote awareness of laws against improper insider trading, and do not tolerate it.
- We offer no payments or favors to influence others to do something wrong.
- We value open and fair competition and respect the rights of our customers, suppliers and competitors just as we expect our rights to be respected.
- We actively encourage every TI employee, officer and director to recognize and report any concern about possible illegal or unethical behavior, and we ensure that such reports made in good faith will be acted upon responsibly and without retaliation.
- We create a work place where we feel free to express our opinions and to raise questions and concerns in a safe and supportive environment, without fear of harassment, retribution or retaliation by peers or managers.[23]

Discuss the similarities and differences in TI's Code and the American Marketing Association's "Statement of Ethics: Ethical Norms and Values for Marketers" at http://www.marketingpower.com.

Source: Courtesy of Texas Instruments

REVIEW LEARNING OUTCOME

LO 8 Discuss the unique aspects of business buying behavior



the total business value they generate over time.

To achieve this goal, the firm must be able to sort customers into two or more groups based on their value. It must also create and apply policies that govern how service will be allocated among groups. Policies might establish which customers' phone calls get "fast tracked" and which customers are directed to use the Web and/or voice self-service, how specific e-mail questions are routed, and who is given access to online chats and who isn't.[24]

Providing different customers with different levels of service is a very sensitive matter. It must be handled carefully and discreetly to avoid offending lesser value, but still important customers.

$1 < trillion: total U.S. B2B commerce for 2008

core companies in the Toyota Group keiretsu > **14**

170 < companies that receive preferential treatment from the Toyota Group keiretsu

wholesalers operating in the United States > **500,000**

$600 billion < amount the U.S. federal government spends each year on goods and services

NAICs economic sectors > **20**

$200 billion < size of the contract the Pentagon awarded to Lockheed Martin to build 3,000 jet fighter planes

28 < orthopedic companies in tiny Warsaw, Indiana

people employed by orthopedic companies in Warsaw's seven-mile radius > **6,500**

20,000 < transactions made each week on Exostar—the online exchange of the aerospace industry

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Review and Applications

LO 1 Describe business marketing. Business marketing provides goods and services that are bought for use in business rather than for personal consumption. Intended use, not physical characteristics, distinguishes a business product from a consumer product.

WRITING

1.1 As the marketing manager for Huggies diapers made by Kimberly-Clark, you are constantly going head-to-head with Pampers, produced by rival Procter & Gamble. You are considering unlocking the potential of the business market to increase your share of the disposable diaper market, but how? Write an outline of several ways you could transform this quintessentially consumer product into a successful business product as well.

LO 2 Describe the role of the Internet in business marketing. The rapid expansion and adoption of the Internet have made business markets more competitive than ever before. The number of business buyers and sellers using the Internet is rapidly increasing. Firms are seeking new and better ways to expand markets and sources of supply, increase sales and decrease costs, and better serve customers. Marketers are becoming more sophisticated in their use of the Internet and are developing quantitative methods that can be used to better measure online success.

ONLINE

2.1 How could you use the Web site **http://www.BtoBonline.com** to help define a target market and develop a marketing plan?

2.1 Reconsider question 1.1. How could you use the Internet in your business marketing of Huggies diapers?

LO3 **Discuss the role of relationship marketing and strategic alliances in business marketing.** Relationship marketing entails seeking and establishing long-term alliances or partnerships with customers. A strategic alliance is a cooperative agreement between business firms. Firms form alliances to leverage what they do well by partnering with others that have complementary skills.

3.1 Why is relationship or personal selling the best way to promote in business marketing?

LO4 **Identify the four major categories of business market customers.** Producer markets consist of individuals and for-profit organizations that buy products for use in producing other products, as components of other products, or in facilitating business operations. Reseller markets consist of wholesalers and retailers that buy finished products to resell for profit. Government markets include federal, state, county, and city governments that buy goods and services to support their own operations and serve the needs of citizens. Institutional markets consist of very diverse nonbusiness institutions whose main goals do not include profit.

4.1 Understanding businesses is key to business marketing. Publications like *Manufacturing Automation, Computer Weekly, Power Generation Technology & Markets,* and *Biotech Equipment Update* can give you insights into many business marketing concepts. Research the industrial publications to find an article on a business marketer that interests you. Write a description of the company using as many concepts from the chapter as possible. What major category or categories of business market customers does this firm serve?

ONLINE

4.2 What do you have to do to get a government contract? Check out the Web sites **http://www.fedbizopps.gov** and **http://www.governmentbids.com** to find out. Does it seem worth the effort?

LO5 **Explain the North American Industry Classification System.** The NAICS provides a way to identify, analyze, segment, and target business and government markets. Organizations can be identified and compared by a numeric code indicating business sector, subsector, industry group, industry, and country industry. NAICS is a valuable tool for analyzing, segmenting, and targeting business markets.

ONLINE

5.1 Explain how a marketer can use the Web site **http://www.census.gov/epcd/ www/naics.html** to convert SIC data to the NAICS.

5.2 Pick a product and determine its NAICS code. How easy is it to trace the groups and sectors?

LO6 **Explain the major differences between business and consumer markets.** In business markets, demand is derived, price-inelastic, joint, and fluctuating. Purchase volume is much larger than in consumer markets, customers are fewer in number and more geographically concentrated, and distribution channels are more direct. Buying is approached more formally using professional purchasing agents, more people are involved in the buying process, negotiation is more complex, and reciprocity and leasing are more common. And, finally, selling strategy in business markets normally focuses on personal contact instead of advertising.

6.1 How might derived demand affect the manufacturing of an automobile?

6.2 Your boss has just asked you, the company purchasing manager, to buy new computers for an entire department. Since you have just recently purchased a new home computer, you are well-educated about the various products available. How will your buying process for the company differ from your recent personal purchase?

LO7 **Describe the seven types of business goods and services.** Major equipment includes capital goods, such as heavy machinery. Accessory equipment is typically less expensive and shorter-lived than major equipment. Raw materials are extractive or agricultural products that have not been processed. Component parts are finished or near-finished items to be used as parts of other products. Processed materials are used to manufacture other products. Supplies are consumable and not used as part of a final product. Business services are intangible products that many companies use in their operations.

7.1 In small groups, brainstorm examples of companies that feature the products in different business categories. (Avoid examples already listed in the chapter.) Compile a list of ten specific business products including at least one in each category. Then match up with another group. Have each group take turns naming a product while the other group identifies its appropriate category. Discuss your discrepancies and try to resolve them. Some identified products may appropriately fit into more than one category.

LO8 **Discuss the unique aspects of business buying behavior.** Business buying behavior is distinguished by five fundamental characteristics. First, buying is normally undertaken by a buying center consisting of many people of varying authority levels. Second, business buyers typically evaluate alternative products and suppliers based on quality, service, and price—in that order. Third, business buying falls into three general categories: new buys, modified rebuys, and straight rebuys. Fourth, the ethics of business buyers and sellers are often scrutinized. Fifth, customer service before, during, and after the sale plays a big role in business purchase decisions.

8.1 A colleague has sent you an e-mail seeking your advice as he attempts to sell a new voice-mail system to a local business. Send him a return e-mail describing the various people who might influence the customer's buying decision. Be sure to include suggestions for dealing with the needs of each of these individuals.

8.2 Intel Corporation supplies microprocessors to Hewlett-Packard for use in its computers. Describe the buying situation in this relationship, keeping in mind the rapid advance of technology in this industry.

Key Terms

accessory equipment	218
business-to-business electronic commerce	206
business-to-business online exchange	216
business marketing	206
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Exercises

APPLICATION EXERCISE

Purchasing agents are often offered gifts and gratuities. Increasingly, though, companies are restricting the amount and value of gifts that their purchasing managers can accept from vendors. The idea is that purchasing managers should consider all qualified vendors during a buying decision instead of only those who pass out great event tickets. This exercise asks you to consider whether accepting various types of gifts is ethical.[25]

Activities

1. Review the following list of common types of gifts and favors. Put a checkmark next to the items that you think it would be acceptable for a purchasing manager to receive from a vendor.

—Advertising souvenirs
—Clothing
—Discounts on personal purchases
—Golf outings
—Large appliances
—Automobiles
—Dinners
—Food and liquor
—Holiday gifts
—Loans of money

—Lunches
—Tickets (sports, theater, amusement parks, etc.)
—Vacation trips
—Small-value appliances
—Trips to vendor plants

2. Now look at your list of acceptable gifts through various lenses. Would your list change if the purchasing manager's buying decision involved a low-cost item (say, pens)? Why or why not? What if the decision involved a very expensive purchase (like a major installation)?
3. Form a team and compare your lists. Discuss (or debate) any discrepancies.

ETHICS

ETHICS EXERCISE

Cameron Stock, purchasing manager for a sports equipment manufacturer, is responsible for buying $5 million of supplies every year. He keeps a preferred list of certified suppliers, who are awarded a large percentage of his business. Cameron has been offered a paid weekend for two in Las Vegas as a Christmas present from a supplier with whom he has done business for a decade and built a very good relationship.

Questions

1. Would it be legal and ethical for Cameron Stock to accept this gift?
2. How is this addressed in the AMA Statement of Ethics? Go to the AMA Web site at **http://www.marketingpower.com** and reread the Statement of Ethics. Write a brief paragraph summarizing where the AMA stands on the issue of supplier gifts.

Case Study: Camelbak

THEY'VE GOT YOUR 'BAK

In 1989, Michael Eidson probably never imagined that his homemade, do-it-yourself fix for dehydration during long cycling races would evolve into the world's premier hydration device for outdoor enthusiasts, soldiers, and law enforcement personnel. That is exactly what happened to the CamelBak backpack, however.

The first version, which used medical tubing to flow water from an intravenous drip bag that was insulated by a sock and strapped to the back of his shirt, was born as most inventions are—out of necessity. The special pack made it possible for Eidson to take in fluids while sitting upright without having to sacrifice speed by reaching down for a water bottle during a race. The packs gained fame during the 1991 Gulf War as extreme sports enthusiasts in the U.S. Special Forces carried their personal CamelBaks into combat during Desert Storm. Thereafter, the CamelBak name would be forever associated with extreme performance and the U.S. Armed Forces.

By 1995, Eidsen sold the company for $4 million. Its buyer, Kransco, introduced the first camouflaged models, and the packs continued to gain acclaim. In 1999, two years after buying his first CamelBak pack, cyclist Chuck Hunter left Lockheed Martin to join the upstart company in hopes of growing its military business. He promptly moved the company to the Sonoma Valley, built a research and development center, and leveraged his experience in the defense industry to launch a military-specific line of packs.

Hunter partnered with DuPont to help CamelBak develop the Low Infrared Reflective (LIRR) system. LIRR applies specially developed materials to a pack's compartments, buckles, and straps to shield soldiers from enemy detection systems. As advanced identification and kill technologies are increasingly being deployed on the battlefield, individual protection applications like the LIRR will be the camouflage of tomorrow.

Other CamelBak innovations include the WaterBeast reservoir, a fluid storage system that boasts 30 percent more rigidity than other packs on the market. The WaterBeast has the ability to withstand lengthy field engagements, aided by its silver-ion reservoir and tube linings that eliminate 99.99 percent of all fungus and bacteria in the water delivery system. The WaterBeast reservoir is now a standard feature on all CamelBak packs, as is the company's proprietary drinking nozzle, or bite valve, which must withstand 10,000 compressions to guarantee it will last through three years of combat use.

Another CamelBak first is its CBR 4.0 pack system, which is specially designed to perform under chemical or biological weapons attack. The CBR 4.0 took five years to develop, and like all CamelBak military and law enforcement products, it was created to meet the specific requests and requirements of the target market. Since its introduction in 2005, the U.S. Special Forces, New York Police Department, U.S. Secret Service, Department of Health and Human Services, and a myriad of HAZMAT, law enforcement, and government agencies from around the world have adopted and deployed the CBR 4.0.

Though CamelBak specializes in offering extreme performance packs for the military, industrial, and professional markets, it also sells a variety of products for hunting, extreme sports, recreational, and "light" law enforcement applications. Having claimed more than 90 percent of the military market for hydration packs, product manager Shawn Cullen likens CamelBak to Kleenex: "Everyone calls a hydration system a CamelBak," he says. Ironically, the company's biggest customer is its biggest competitor. While it continues to use CamelBaks, the U.S. Army is working with a former supplier to develop its own version, most likely in an attempt to reduce costs.

At prices up to $200 for combat-ready systems, one thing CamelBaks aren't is cheap. But then again, neither is CamelBak itself. Its strong product lines, history of innovation, secure strategic relationships, and dominance in government and institutional markets drove its value to over $200 million when investment bank Bear Stearns Company bought the outfit from Kransco in 2003—not bad for a product that started life as an intravenous fluid bag wrapped in a sock.[26]

Questions

1. Discuss how business relationships and strategic partnerships have helped to increase the value of CamelBak's products and the business itself.
2. What type(s) of business market customers does CamelBak sell to?
3. Review the types of demand that most influence business markets. Which ones do you think are most important for CamelBak to consider in its marketing strategy? Why?
4. What type of business product is a CamelBak backpack?

Company Clips

READYMADE—MAKING BUSINESS RELATIONSHIPS

Like most periodicals, ReadyMade relies on advertisers for much of its revenue. Finding companies interested in advertising in the magazine and cultivating those relationships is an important component of making the company successful. ReadyMade must constantly market its product to potential investors through personal contact and solicitation. ReadyMade also must develop relationships with distributors and other businesses that will directly or indirectly promote the magazine and help make it successful. As you watch this video, notice the strategies that Darci Andresen describes as she explains the process she goes through as head of Advertising Sales & Special Promotions when seeking new advertisers.

Questions

1. When marketing to potential advertisers, what strategies could ReadyMade use to promote itself without having to rely on hard statistics about its readers?
2. What sort of strategic alliances does ReadyMade maintain? In what ways are these partnerships beneficial to the magazine?
3. Go to ReadyMade's Web site, www.readymade.com. What evidence do you see of its business partnerships? How does it use its Web site to market itself to businesses?

Marketing & You Results

A high score indicates that you found the salesperson to be credible and concerned about your needs. Because you found the salesperson to be open and concerned, you had a higher level of trust in the salesperson than did someone with a lower score. As you read in Chapter 6, trust is an important element in building strategic alliances and in cultivating business clients.

CHAPTER 8

Segmenting and Targeting Markets

Learning Outcomes

LO1 Describe the characteristics of markets and market segments

LO2 Explain the importance of market segmentation

LO3 Discuss criteria for successful market segmentation

LO4 Describe the bases commonly used to segment consumer markets

LO5 Describe the bases for segmenting business markets

LO6 List the steps involved in segmenting markets

LO7 Discuss alternative strategies for selecting target markets

LO8 Explain one-to-one marketing

LO9 Explain how and why firms implement positioning strategies and how product differentiation plays a role

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LO 1

Market Segmentation

The term *market* means different things to different people. We are all familiar with the supermarket, stock market, labor market, fish market, and flea market. All these types of markets share several characteristics. First, they are composed of people (consumer markets) or organizations (business markets). Second, these people or organizations have wants and needs that can be satisfied by particular product categories. Third, they have the ability to buy the products they seek. Fourth, they are willing to exchange their resources, usually money or credit, for desired products. In sum, a **market** is (1) people or organizations with (2) needs or wants and with (3) the ability and (4) the willingness to buy. A group of people or an organization that lacks any one of these characteristics is not a market.

market
People or organizations with needs or wants and the ability and willingness to buy.

market segment
A subgroup of people or organizations sharing one or more characteristics that cause them to have similar product needs.

market segmentation
The process of dividing a market into meaningful, relatively similar, and identifiable segments or groups.

Within a market, a **market segment** is a subgroup of people or organizations sharing one or more characteristics that cause them to have similar product needs. At one extreme, we can define every person and every organization in the world as a market segment because each is unique. At the other extreme, we can define the entire consumer market as one large market segment and the business market as another large segment. All people have some shared characteristics and needs, as do all organizations.

From a marketing perspective, market segments can be described as somewhere between the two extremes. The process of dividing a market into meaningful, relatively similar, and identifiable segments or groups is called **market segmentation**. The purpose of market segmentation is to enable the marketer to tailor marketing mixes to meet the needs of one or more specific segments.

Exhibit 8.1 illustrates the concept of market segmentation. Each box represents a market consisting of seven individuals. This market might vary as follows: one

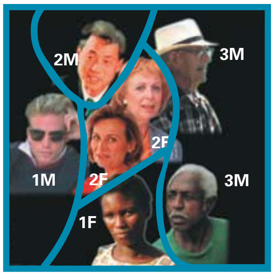
Exhibit 8.1
Concept of Market Segmentation

No market segmentation

Fully segmented market

Market segmentation by gender: M, F

Market segmentation by age group: 1, 2, 3



Market segmentation by gender and age group

Marketing & You

Please note your opinion on each of the following questions.

Using the following scale, enter your opinion.

1	2	3	4	5	6
Strongly agree					Strongly disagree

— I frequently have trouble making ends meet.

— My budgeting is always tight.

— I often have to spend more money than I have available.

— I do not consider myself financially well off.

— I am generally on a tight budget.

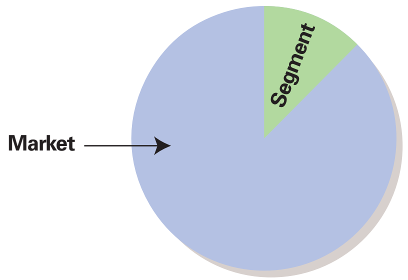
— Meeting an unexpected expense of $1,000 would be a financial hardship.

Total your score. Now, read the chapter and find out what your score means at the end

From Scale #646, Marketing Scales Handbook, G. Bruner, K. James, H. Hensel, eds. Vol. III. © by American Marketing Association.

REVIEW LEARNING OUTCOME

LO 1 Describe the characteristics of markets and market segments



homogeneous market of seven people; a market consisting of seven individual segments; a market composed of two segments based on gender; a market composed of three age segments; or a market composed of five age and gender market segments. Age and gender and many other bases for segmenting markets are examined later in this chapter.

LO 2
The Importance of Market Segmentation

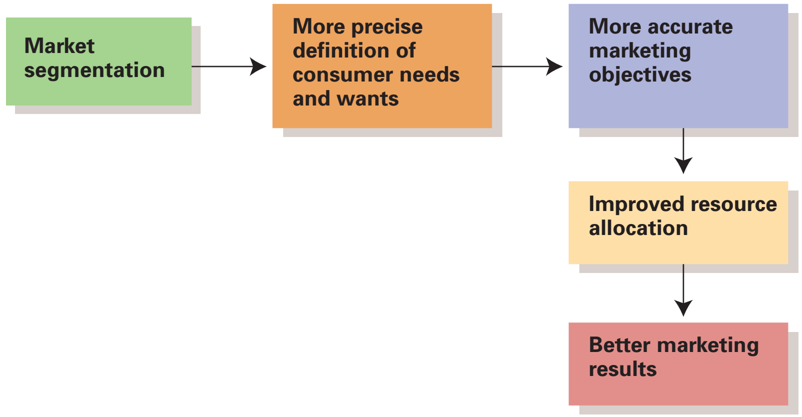
Until the 1960s, few firms practiced market segmentation. When they did, it was more likely a haphazard effort than a formal marketing strategy. Before 1960, for example, the Coca-Cola Company produced only one beverage and aimed it at the entire soft drink market. Today, Coca-Cola offers over a dozen different products to market segments based on diverse consumer preferences for flavors and calorie and caffeine content. Coca-Cola offers traditional soft drinks, energy drinks (such as POWERade), flavored teas, fruit drinks (Fruitopia), and water (Dasani).

Market segmentation plays a key role in the marketing strategy of almost all successful organizations and is a powerful marketing tool for several reasons. Most importantly, nearly all markets include groups of people or organizations with different product needs and preferences. Market segmentation helps marketers define customer needs and wants more precisely. Because market segments differ in size and potential, segmentation helps decision makers to more accurately define marketing objectives and better allocate resources. In turn, performance can be better evaluated when objectives are more precise.

Chico's, a successful women's fashion retailer, thrives by marketing to women aged 35 to 55 who like to wear comfortable, yet stylish clothing. It sells private-label clothing in just a few nonjudgmental sizes: zero (regular sizes 4–6), one (8–10), two (10–12), and three (14–16). Another example is Wal-Mart, which revamped some of its stores to appeal to six different segments of the market: suburban/affluent; urban; multicultural; Hispanic; baby boomer; rural. Stores targeting baby boomers devote more room to pet supplies, baby clothes, and home accessories. Stores catering to Hispanic groups have expanded financial services and use more bilingual language on signs.[1]

REVIEW LEARNING OUTCOME

LO 2 Explain the importance of market segmentation



LO 3
Criteria for Successful Segmentation

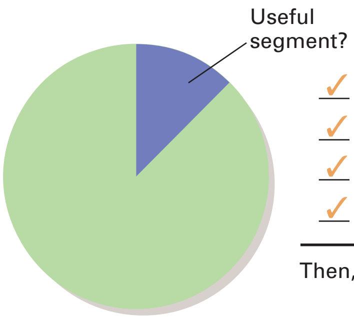
Marketers segment markets for three important reasons. First, segmentation enables marketers to identify groups of customers with similar needs and to analyze the characteristics and buying behavior of these groups. Second, segmentation provides marketers with information to help them design marketing mixes specifically matching the characteristics and desires of one or more segments. Third, segmentation is consistent with the marketing concept of satisfying customer wants and needs while meeting the organization's objectives.

To be useful, a segmentation scheme must produce segments that meet four basic criteria:

- *Substantiality:* A segment must be large enough to warrant developing and maintaining a special marketing mix. This criterion does not necessarily mean that a segment must have many potential customers. Marketers of custom-designed homes and business buildings, commercial airplanes, and large computer systems typically develop marketing programs tailored to each potential customer's needs. In most cases, however, a market segment needs many potential customers to make commercial sense. In the 1980s, home banking failed because few people owned personal computers. Today, many people own computers, and home banking is a thriving industry.
- *Identifiability and measurability:* Segments must be identifiable and their size measurable. Data about the population within geographic boundaries, the number of people in various age categories, and other social and demographic characteristics are often easy to get, and they provide fairly concrete measures of segment size. Suppose that a social service agency wants to identify segments by their readiness to participate in a drug and alcohol program or in prenatal care. Unless the agency can measure how many people are willing, indifferent, or unwilling to participate, it will have trouble gauging whether or not there are enough people to justify setting up the service.
- *Accessibility:* The firm must be able to reach members of targeted segments with customized marketing mixes. Some market segments are hard to reach—for example, senior citizens (especially those with reading or hearing disabilities), individuals who don't speak English, and the illiterate.
- *Responsiveness:* As Exhibit 8.1 illustrates, markets can be segmented using any criteria that seem logical. Unless one market segment responds to a marketing mix differently from other segments, however, that segment need not be treated separately. For instance, if all customers are equally price-conscious about a product, there is no need to offer high-, medium-, and low-priced versions to different segments.

REVIEW LEARNING OUTCOME

LO3 Discuss criteria for successful market segmentation



✓ Substantial
✓ Identifiable and measurable
✓ Accessible
✓ Responsive

Then, yes: use segmentation

LO4

Bases for Segmenting Consumer Markets

segmentation bases (variables) Characteristics of individuals, groups, or organizations.

Marketers use **segmentation bases, or variables,** which are characteristics of individuals, groups, or organizations, to divide a total market into segments. The choice of segmentation bases is crucial because an inappropriate segmentation strategy may lead to lost sales and missed profit opportunities. The key is identifying bases that will produce substantial, measurable, and accessible segments that exhibit different response patterns to marketing mixes.

Markets can be segmented using a single variable, such as age group, or several variables, such as age group, gender, and education. Although less precise, single-variable segmentation has the advantage of being simpler and easier to use than multiple-variable segmentation. The disadvantages of multiple-variable segmentation are that it is often harder to use than single-variable segmentation; usable secondary data are less likely to be available; and as the number of segmentation bases increases, the size of individual segments decreases. Nevertheless, the current trend is toward using more rather than fewer variables to segment most markets. Multiple-variable segmentation is clearly more precise than single-variable segmentation.

Consumer goods marketers commonly use one or more of the following characteristics to segment markets: geography, demographics, psychographics, benefits sought, and usage rate.

GEOGRAPHIC SEGMENTATION

geographic segmentation Segmenting markets by region of a country or the world, market size, market density, or climate.

demographic segmentation Segmenting markets by age, gender, income, ethnic background, and family life cycle.

Geographic segmentation refers to segmenting markets by region of a country or the world, market size, market density, or climate. Market density means the number of people within a unit of land, such as a census tract. Climate is commonly used for geographic segmentation because of its dramatic impact on residents' needs and purchasing behavior. Snow blowers, water and snow skis, clothing, and air-conditioning and heating systems are all have varying appeal, depending on climate.

Consumer goods companies take a regional approach to marketing for four reasons. First, many firms need to find new ways to generate sales in sluggish and intensely competitive markets. Second, computerized checkout stations with scanners give retailers an accurate assessment of which brands sell best in their region. Third, many packaged-goods manufacturers are introducing new regional brands intended to appeal to local preferences. Fourth, a regional approach enables consumer goods companies to react more quickly to competition. For example, research showed Saks Fifth Avenue's customers differ significantly at stores around the country. At the New York store, Saks' core shopper is a mid-40s woman with a classic style. By contrast, core shoppers at its Birmingham, Alabama store are more brand-savvy, fashion-loving, and slightly younger.[2] IKEA discovered that its Japanese customers live in small spaces. In response, its store displays suggest ways for customers to fit IKEA products into the cramped spaces of typical Japanese homes.[3]

© AP PHOTO/CHITOSE SUZUKI

Saks' marketing analysts found that the merchandise at their flagship Saks' Fifth Avenue store in New York City doesn't necessarily appeal to Saks customers nationwide. To bolster sales, Saks' marketing analysts use geodemographic research to determine what merchandise will appeal to customers in each of its 54 retail stores, from Birmingham, Alabama, to Bellevue, Washington.

DEMOGRAPHIC SEGMENTATION

Marketers often segment markets on the basis of demographic information because it is widely available and often related to consumers' buying and consuming behavior. Some common bases of demographic segmentation are age, gender, income, ethnic background, and family life cycle.

Age Segmentation

Marketers use a variety of terms to refer to different age groups. Examples include newborns, infants, young children, tweens, teens and young adults, (Generation Y),

ETHICS in Marketing

Targeting Kids 8-and-under

Marketers have long advertised their products to adolescents, tweens and grade-schoolers. However, three quarters of U.S. children watching ads for toys, athletic shoes, and snack food each day are under 6 years old, and 43 percent are younger than 2. According the American Psychological Association, the concept of a "commercial" means nothing to children under age 9. They perceive ad claims facts because they can't understand the motives and persuasive intent behind commercials.

Some marketers argue that they are targeting their parents, not the kids themselves. For example, Josef Mandelbaum, president of American Greetings Intellectual Properties, owner of Care Bears and Strawberry Shortcake, claims that television shows based on these characters reinforce the brands to kids, but don't target them with advertising. Others such as Disney, McDonald's, and Hasbro openly admit that 5- and 6-year-old children are a reasonable target for their products. Kids even get a dose of advertising-related messages before and at school. The trip to school may include Bus Radio with ads from companies such as News Corp., Disney, Cartoon Network, and AT&T. Corporate sponsor logos, branded vending machines, and book covers sponsored by PepsiCo, Hasbro, and Ronald McDonald can be found on school grounds.

Research confirms that kids are learning to be consumers early in life. A study by the Campaign for a Commercial-Free Childhood (CCFC) found that children between 4 and 12 years old spent $30 billion in 2002, up from $6.1 billion in 1989. And, according to another study, kids influence another $600 billion a year in family spending. One third of kids between 4 and 6 years old have their own DVD player, a handheld videogame player, and a television set in their rooms. Ninety percent of these children use some form of screen media every day for an average of two hours. Thus, kids form a large target market, and they are easy for companies to reach with advertising and product-related messages.

Marketers are spending $15 billion a year to reach young children, who now see roughly 40,000 television commercials each year. Other marketing activities range from creation of the McDonald's Happy Meal to interactive activities kids can find online. For example, Pepperidge Farm offers "Goldfish Central," a Web site where "Finn," a spokes-fish for the fish-shaped snack food, invites kids into a virtual world of adventures featuring his many fish friends.

CCFC and other advocacy groups have taken the position that there is no moral, ethical or social justification for advertising to children. The issue is not only the presence of kid-focused advertising but also of brand integration into entertainment, linking kids' movies and snack foods, and product peddling by licensed characters. The solution the advocacy groups support is not regulation, but a total ban on kid marketing, like that in many European countries.

On the other side, marketers claim that it would be nearly impossible to ensure that kids don't view advertising given the proliferation of media. Some marketers argue that parents should act as filters for media content and educate their children about ads. Others claim that advertising to children under 8 can be done responsibly. Julie Halpin, CEO of the Geppetto Group, a New-York based marketing firm that works with companies such as Coca Cola, Reebok and Unilever, maintains that they serve the client's business objectives and the best interests of kids. Some companies have taken measures to be responsible advertisers to kids. Fisher Price, which aims about 20 percent of its ads to children as young as 3 or 4, tests its marketing on focus groups of kids and parents, using the latter's input to guide content and approach.

Is it acceptable for marketers to target young children with advertising messages? If so, what should the content and approach of these messages be? If not, how would you implement regulations or a ban on kid marketing?

SOURCE: Based on T. L. Stanley, "Babes in Brandland," *Brandweek*, October 15, 2007, 29-30.

adults (Generation X), baby boomers, and seniors. Age segmentation can be an important tool, as a brief exploration of the market potential of several age segments illustrates.

Through allowances, earnings, and gifts, children account for, and influence, a great deal of consumption. For example, there are about 20 million so-called tweens (ages 9–12) in the United States. This group spends over $20 billion per year and influences how another $200 billion is spent.[4] Tweens desire to be kids, but also want some of the fun of being a teenager. Many retailers such as Limited Too serve this market with clothing that is similar in style to that worn by teenagers and young adults. The Generation Y market has purchasing power of more than $200 billion a year.[5] Teens spend most of their money on clothing, entertainment, and food. This group is aware of brands and also of marketing strategies.

Therefore, obvious marketing techniques won't work. Teens consider brands like iPod, American Eagle Outfitters, Facebook, and MTV to be not only their favorites, but as defining their generation.[6] They are environmentally conscious, and say they would spend more on environmentally-conscious brands or in environmentally friendly stores.[7] Teenagers also spend lots of money online. In 2006, they spent $13 billion on the Web, accounting for 3 percent of all online sales in the United States. Teens also have a strong influence on household items their parents purchase online.[8]

Generation X is the group that was born after the baby boomers. Members of Generation X tend to be disloyal to brands and skeptical of big business. Many of them are becoming parents, and they listen to input from and think of their families when making purchasing decisions. Xers look for experience, not just products. For example, Starbucks developed a market for expensive coffee by incorporating it in a coffee-drinking ambiance that appeals to this consumer segment.[9]

People born between 1946 and 1964 are often called "baby boomers." Boomers spend $2.1 trillion a year, accounting for half of all spending in the U.S. For the next 18 years, one baby boomer will turn 60 every seven seconds. They make up 49 percent of affluent households, and they want attention and service when they shop.[10] Baby boomers think of themselves as trailblazers, so marketers can appeal to their desire to break away from the norm. The ad for American Express' Ameriprise financial services does this by saying "You changed everything that came before you. That was you then. . . that's still you now."[11] Great challenges await marketers who target boomers. Unlike yesterday's generation of 60-year-olds, the boomers refuse to believe they're aging, so marketers should avoid suggesting it. Rather, they must appeal to boomers' interests, lifestyles, and values. Companies as diverse as Whirlpool, Gap, Moen, Fila, and OXO do this with great success. The president of OXO, the company that makes Good Grips cooking utensils with the thick black handles, says, "The last thing they want is the kind of patronizing, help-me-do-something kind of tools. We have almost a cult-like following among older consumers. At the same time, we have just as strong a following from people in the 20-to-40 age range because the products look cool."[12]

Consumers in their early 60s and older represent people who are part of the War Generation (ages 61 to 66), the Depression Generation (ages 67 to 76) and the G. I. Generation (age 77 and up). Collectively, they are sometimes called the "Golden Generation"(a term coined by Focalyst, a research and consultancy firm focused on older consumers). Many in this group view retirement not as a passive time, but as an opportunity for learning, traveling, volunteering, and spending time with family and friends. They are healthier and living longer than older consumers 20 years ago. However, marketers should be aware that physical changes in hearing, eyesight and mobility still occur in this segment. The Hartford Financial Service Group provides auto and homeowner insurance to AARP members. The company's voice self-service system has a low-pitched male voice that is easier for their older members to hear. The Hartford trains its employees to deal with conditions of aging, including hearing impairments, and has nine gerontologists on staff to advise on such issues.[13]

Gender Segmentation

In the United States, women handle 75 percent of family finances and make or influence 80 percent of consumer purchases. They buy 51 percent of the new electronics sold, 75 percent of over-the-counter drugs, and 65 percent of new cars. Women make purchase decisions about a huge variety of goods and services, not just the packaged goods that have traditionally been marketed to them.[14]

In the new car market, women are increasingly making buying decisions, and car makers are starting to cater to them. Ford offers eye shadow and nail polish complementing the color of its cars. General Motors sponsors cooking classes

IMAGE COURTESY OF THE ADVERTISING ARCHIVES

Many companies have profited from redesigning traditionally feminine products and marketing them towards men. Here, Lancôme advertises an anti-wrinkle cream that has been packaged to appeal to men.

and holds fashion shows in its traveling auto displays, and Toyota is constructing play areas for children and encouraging its dealers to redecorate their restrooms more tastefully.[15] Other marketers that traditionally focused on males are also recognizing the potential of the female market segment. For example, the number of women shopping at hardware stores such as Home Depot and Lowe's Home Improvement Warehouse has risen in recent years. A survey by Ace Hardware revealed that 42 percent of its customers are women, and that they spend 30 to 40 percent more than men per visit. Home improvement stores are reaching out to women by creating a grocery store–type experience with wide, well-lit aisles, clear signage, and instructions for product use.[16] Home Depot is testing a new store concept designed to attract women shoppers. These stores will focus on upscale home décor and organization, using extravagant showrooms and extensive product selection.[17]

Similarly, other brands that have targeted men, such as Gillette razors and Rogaine baldness remedy, are trying to attract women. For example, athletic apparel manufacturers such as Nike and Reebok have typically targeted men, and when they did target women, simply copied the hard-edged, sports-marketing strategies they used for men. Mindy Grossman, vice president of global apparel for Reebok, says, "We were taking the men's formula—big athlete, big marketing—and trying to apply it to women. But that's not how she [sic] responds." Reebok developed apparel for all kinds of women's activities which, more often than not, include fitness dance and yoga instead of traditional, competitive sports.[18]At the same time marketers that traditionally focused almost exclusively on women have recognized the important potential of the male segment. For example, males are increasingly involved in wedding planning, deciding on everything from locations, seating plans, and table decorations, to wedding cakes and keepsakes for guests. As men get more involved in their weddings, businesses such as engagement consultants, resorts, and spas are beginning to create special packages designed to attract men.[19] To illustrate, the Fairmont Princess Resort in Scottsdale, Arizona, hired a cultural anthropologist when it wanted to target men alongside its female clientele. The researcher found intrinsic differences in the way men and women approach spas, prompting resort to:

- Use darker woods and colors to create a club-like ambiance so men wouldn't feel they were entering female territory
- Install televisions in locker rooms (to reduce awkwardness of wearing spa gear)
- Develop customized packages, including "Keep Your Shorts On" and "Golf Performance Treatment"
- Reposition the "European Facial," as translated for men, into the "Barber Facial"[20]

Marketers of products including clothing, cosmetics, personal-care items, magazines, jewelry, and footwear still commonly segment markets by gender. Sports Clips hair salon appeals to men and boys. The waiting room features a TV with a 52-inch screen, and customers can buy sports memorabilia, pro team caps, and college charcoal grills with their hair-care products. Men shopping alone make up about 18 percent of grocery shoppers. A recent study found that compared to women, men place a higher priority on location and convenience, don't like loyalty cards, and often stray from their lists, creating opportunities for grocers to encourage impulse buys.[21]

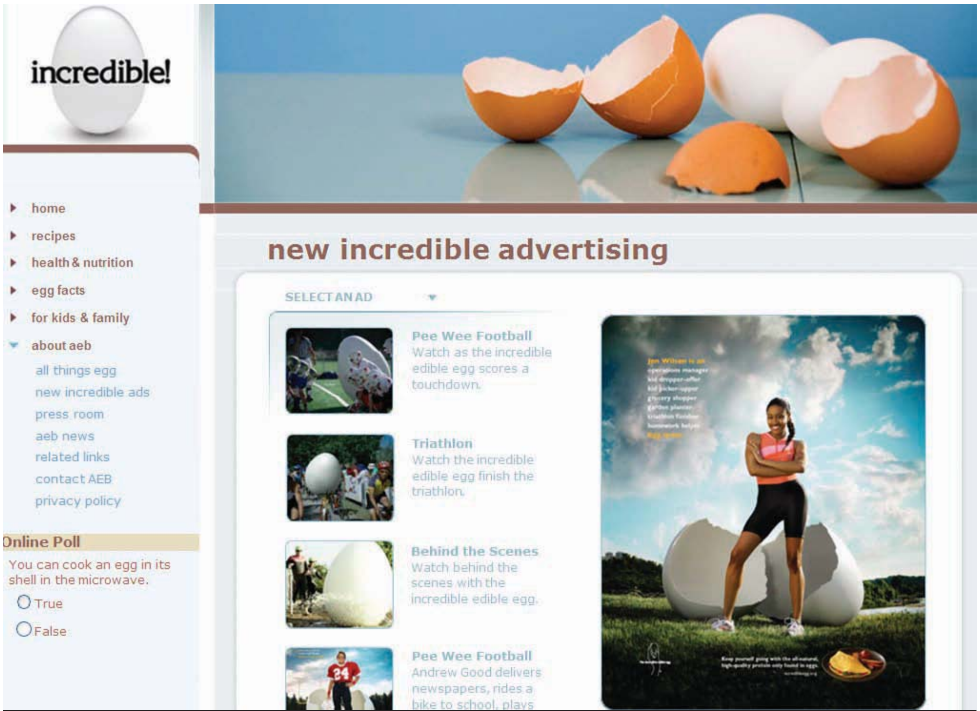
Income Segmentation

Income is a popular demographic variable for segmenting markets because income level influences consumers' wants and determines their buying power. Many markets, including those for housing, clothing, automobiles, and food, are segmented by income. Wholesale club stores like Costco and Sam's Club appeal to many income segments. According to a Nielsen study, affluent households (those earning more than $100,000 annually) are twice as likely to shop warehouse stores than households earning $20,000 or less a year, and an affluent shopper spends, on average, $46 more than the lower income shopper each trip.[22] Lexus has traveled the United States asking wealthy customers what they want, and is developing several new cars costing over $70,000 to appeal to this group.[23] Other companies try to appeal to low income customers. Casual Male has launched a big-and-tall brand of men's apparel aimed at the lower income market. Proctor & Gamble introduced Bounty Basic paper towels and Charmin Basic bath tissue to attract price-sensitive consumers.[24]

Ethnic Segmentation

In the past, ethnic groups in the United States were expected to conform to a homogenized, Anglo-centric ideal. This was evident both in the marketing of mass-marketed products and in the selective way that films, television, advertisements, and popular music portrayed America's diverse population. Until the 1970s, ethnic foods were rarely sold outside specialty stores. The racial barrier in entertainment lasted nearly as long, except for supporting movie and TV roles—often based on stereotypes dating back to the nineteenth century.[25] Growing numbers of ethnic minorities in the U.S., along with increased buying power, have changed this. Hispanic Americans, African Americans, and Asian Americans are the three largest ethnic groups in the United States. In 2006, these three groups accounted for 88 million people, and are expected to represent about a third of the total U.S. population by 2010.[26] Today, companies such as Procter & Gamble, Allstate Insurance, Bank of America, and Reebok have developed multicultural marketing initiatives designed to explore and serve the wants and preferences of U.S. minority groups. Many consumer goods companies spend 5 to 10 percent of their marketing budgets specifically targeting multicultural consumers. This proportion will likely increase as ethnic groups represent larger and larger percentages of the U.S. population.

Experts say that regardless of the segment being targeted, marketers educate themselves about



Successful marketers educate themselves about the consumer they are pursuing, regardless of the segment being targeted. The American Egg Council's ad campaign targets the American mom and includes women of varied segments of the American population.

the consumer they are pursuing, convey a message that is relevant to each particular market, use the Internet to educate ethnic markets about brands and products, and use integrated marketing techniques to reinforce the message. As Catherine Linder, Walgreens divisional vice president and general merchandise manager for beauty and fashion, noted, "Our customers are as diverse as the communities we serve."[27]

The U.S. Census Bureau estimates that the number of Hispanic Americans was 44.3 million in 2006, growing to 47.8 million by 2011. Within this segment exists a variety of nationalities (people come from nearly 24 countries), languages, degrees of acculturation, income, and education levels. The Hispanic segment also is younger than is the total U.S. population.[28] Food retailers should understand not only that Hispanic shoppers like full-flavored products, but also that Mexico has different regional variations in preferences, and that menus and tastes also vary among people from Central and South America.[29] U.S. Cellular knows that their Spanish-speaking customers like to talk with a retail wireless consultant that can explain to them in their language all parts of cellular service. One television ad campaign showed a mother and daughter going from store to store with the daughter explaining and translating at each stop. Once they reach a U.S. Cellular store, the employee makes her feel comfortable by speaking in Spanish. This ad helped to make the company's brand relevant to the Hispanic market.[30]

The African American segment now makes up more than 13 percent of the U.S. population, and will continue to grow. Companies that have been successful in appealing to groups within this segment include Nissan, Merrill Lynch, and AARP. Nissan found that a sense of inclusion among other ethnic groups was preferable to being singled out, so its ad campaign for the Nissan Altima incorporated people of various ethnic backgrounds. Merrill Lynch & Company sponsors community-based events such as the Lasting Foundations: The Art of Architecture in Africa in New York. A membership benefits campaign for AARP recognized that African Americans are not typically close to retirement at age 50. Thus the organization focused on immediate benefits, such as volunteer opportunities, grandparenting programs, and discounts on travel and health care.[31]

Asians in America represent a segment that has higher than average household incomes and education levels than the general population.[32] This group also makes more online purchases a year than African American and Caucasian consumers. More packaged goods companies such as Kraft Foods and Procter & Gamble are showing interest in Asian Americans due to the growth of Asian supermarket chains. At the same time, the number of Asian media is growing rapidly. Los Angeles has nine media choices for Chinese Americans and four for Korean Americans, Atlanta has seven Korean choices and Las Vegas has Filipino and Chinese media.[33]

Family Life-Cycle Segmentation

The demographic factors of gender, age, and income often do not sufficiently explain why consumer buying behavior varies. Frequently, consumption patterns among people of the same age and gender differ because they are in different stages of the family life cycle. The **family life cycle (FLC)** is a series of stages determined by a combination of age, marital status, and the presence or absence of children.

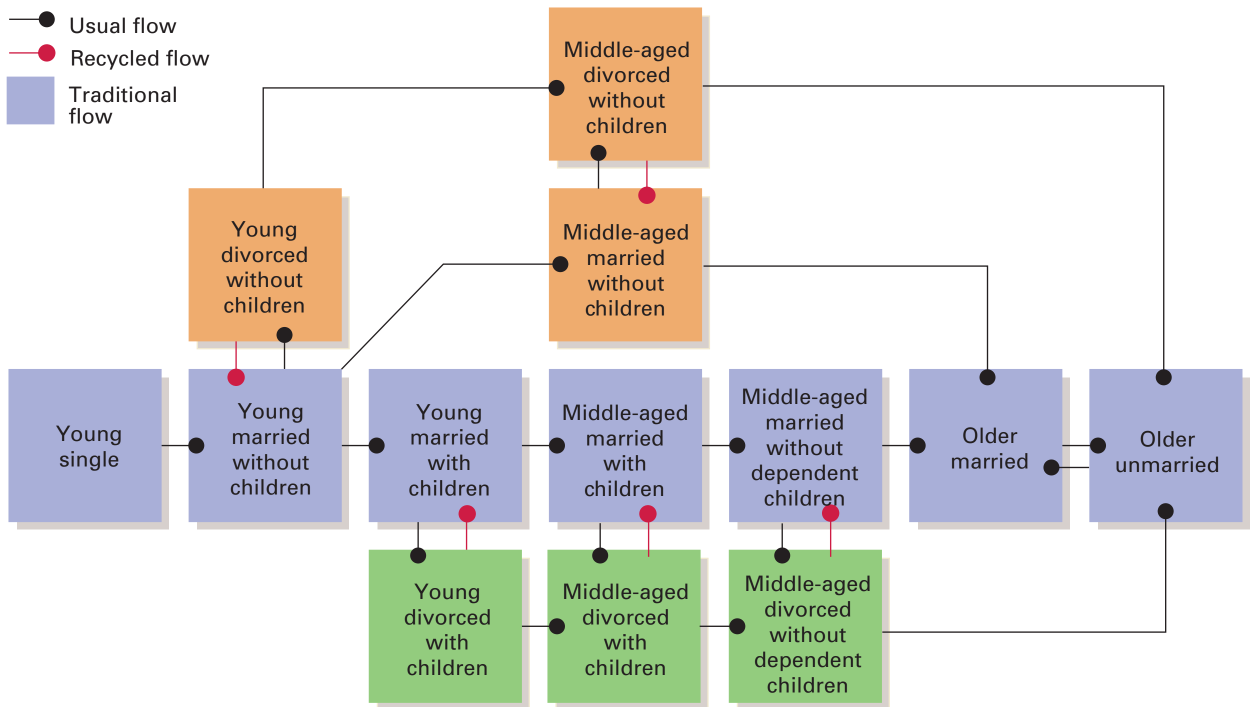
family life cycle (FLC)
A series of stages determined by a combination of age, marital status, and the presence or absence of children.

The life-cycle stage consisting of the married-couple household used to be considered the traditional family in the United States. Today, however, married couples make up just about half of households, down from nearly 80 percent in the 1950s. This means that the 86 million single adults in the United States could soon define the new majority. Already, unmarried Americans make up 42 percent of the workforce, 40 percent of home buyers, and one of the most potent consumer groups on record. Exhibit 8.2 illustrates numerous FLC patterns and shows how families' needs, incomes, resources, and expenditures differ at each stage. The horizontal flow shows the traditional family life cycle. The lower part of the exhibit gives some of the characteristics and purchase patterns of families in each stage of the traditional life cycle. The exhibit also acknowledges that about half of all first marriages end in divorce. When young marrieds move into the young divorced stage, their consumption patterns often revert back to those of the young single stage of the cycle. About four out of five divorced persons remarry by middle age and reenter the traditional life cycle, as indicated by the "recycled flow" in the exhibit.

Consumers are especially receptive to marketing efforts at certain points in the life cycle. Soon-to-be-married couples are typically considered to be most receptive because they are making brand decisions about products that could last longer than their marriages. Women who are pregnant start thinking about healthier lifestyles and are more open to organic foods. As a result, the market for organic food in general, and organic baby food in particular, are growing.[34]

Exhibit 8.2

Family Life Cycle



Young single	**Young married or divorced without children**	**Young married or divorced with children**	**Middle-aged married or divorced with or without children**	**Middle-aged married or divorced without children**	**Older married**	**Older unmarried**
Few financial burdens Fashion opinion leaders Recreation-oriented Buy: basic kitchen equipment, basic furniture, cars, equipment for mating game, vacations	Better off financially than they will be in near future Highest purchase rate and highest average purchase of durables Buy: cars, refrigerators, stoves, sensible and durable furniture, vacations	Home purchasing at peak Liquid assets low Dissatisfied with financial position and amount of money saved Interested in new products Like advertised products Buy: washers, dryers, televisions, baby food, chest rubs, cough medicine, vitamins, dolls, wagons, sleds, skates	Financial position still better More wives work Some children get jobs Hard to influence with advertising High average purchase of durables Buy: new and more tasteful furniture, auto travel, unnecessary appliances, boats, dental	Home ownership at peak Most satisfied with financial position and money saved Interested in travel, recreation, self-education Make gifts and contributions Not interested in new products Buy: vacations, luxuries, home improvements	Drastic cut in income Keep home Buy: medical appliances, medical care, products that aid health, sleep, and digestion	Drastic cut in income Special need for attention, affection, and security Buy: same medical and product needs as other retired group

Research has found that the overriding factor in describing Baby Boomer subsegments is the presence of children in the house. The Nielsen study discovered eight specific segments: four segments with children under 18 represented about 40 percent of the Boomers, and four segments without children represented 60 percent.[35]

PSYCHOGRAPHIC HIC SEGMENTATION

Age, gender, income, ethnicity, family life-cycle stage, and other demographic variables are usually helpful in developing segmentation strategies, but often they don't paint the entire picture. Demographics provide the skeleton, but psychographics add meat to the bones. Psychographic segmentation is market segmentation on the basis of the following variables:

psychographic segmentation Market segmentation on the basis of personality, motives, lifestyles, and geodemographics.

geodemographic segmentation Segmenting potential customers into neighborhood lifestyle categories.

- *Personality:* Personality reflects a person's traits, attitudes, and habits. According to a national survey by Roper, almost half of Americans believe their cars match their personalities. They believe SUVs deliver heady, above-it-all independence, convertables epitomize wind-in-the-hair freedom, and off-roaders signal outdoor adventure. About 25 percent of people surveyed say that their cars make them feel powerful.[36]
- *Motives:* Marketers of baby products and life insurance appeal to consumers' emotional motives—namely, to care for their loved ones. By highlighting economy, reliability, and dependability, carmakers like Subaru and Suzuki target customers with rational motives. Carmakers like Mercedes-Benz, Jaguar, and Cadillac appeal to customers with status-related motives.
- *Lifestyles:* Lifestyle segmentation divides people into groups according to the way they spend their time, the importance of the things around them, their beliefs, and socioeconomic characteristics like income and education. For example, a recent study of baby boomers by Unilever found four segments partially based on lifestyle characteristics: *Savvy Savers* are self-aware, suburban and cosmopolitan, and like to follow cultural and sporting events; *Daily Planners* are kid-centric and environmentally aware; *Plain and Practicals* are conservative, religious, outdoorsy, and self-sufficient; *No-Frills Independents* are loners, have lower income, and tend to be older.[37]
- *Geodemographics:* Geodemographic segmentation clusters potential customers into neighborhood lifestyle categories. It combines geographic, demographic, and lifestyle segmentations. Geodemographic segmentation helps marketers develop programs tailored to prospective buyers who live in small geographic regions, such as neighborhoods, or who have very specific lifestyle and demographic characteristics. H-E-B Grocery Company, a 304-store, Texas-based supermarket chain, specializes in developing its own branded products designed to meet the needs and tastes of specific communities. In the Rio Grande Valley, where summers are hot and many residents lack air conditioning, H-E-B markets its own brand of rubbing oil that cools and moisturizes skin. Along the southern border, the grocer stocks *discos*, large metal disks that Mexican Americans use to cook brisket. Further north, it sells gas grills to Anglo Americans. Stores in predominantly Asian, Latino, or African American neighborhoods carry merchandise specifically selected for each geodemographic target market.

Psychographic variables can be used individually to segment markets or be combined with other variables to provide more detailed descriptions of market segments. One combination approach is the Claritas PRIZM Lifestyle software program that divides Americans into 66 "clusters," or consumer types, all with catchy names. The clusters combine basic demographic data such as age, ethnicity, and income with lifestyle information, such as magazine and sports preferences, taken from consumer surveys. For example, the "Kids and Cul-de-Sacs" group consists of upscale, married couples living with their children in recently built subdivisions. These families have a median household income of $70,233, tend to own a Honda Odyssey, and are likely to spend large sums of money for child-centered products and services such as video games and Chuck E. Cheese. The "Bohemian Mix" cluster is made up of urbanites under age 35. These young singles, couples, students, and professionals have a median income of $51,100, are early adopters in many product categories, and they tend to shop at Banana Republic and read *Vanity Fair* magazine.[38] The program also predicts which neighborhoods across the country these clusters are likely to gather in.

BENEFIT SEGMENTATION

benefit segmentation
The process of grouping customers into market segments according to the benefits they seek from the product.

Benefit segmentation is the process of grouping customers into market segments according to the benefits they seek from the product. Most types of market segmentation are based on the assumption that this variable and customers' needs are related. Benefit segmentation is different because it groups potential customers on the basis of their needs or wants rather than some other characteristic, such as age or gender. The snack-food market, for example, can be divided into six benefit segments, as shown in Exhibit 8.3.

Customer profiles can be developed by examining demographic information associated with people seeking certain benefits. This information can be used to match marketing strategies with selected target markets. The many different types of performance energy bars with various combinations of nutrients are aimed at consumers looking for different benefits. For example, PowerBar is designed for athletes looking for long-lasting fuel, while PowerBar Protein Plus is aimed at those who want extra protein to replenish muscles after strength training. Carb Solutions High Protein Bars are for low-carb dieters; Luna Bars appeal to women who want a bar with fewer calories, soy protein, and calcium; and Clif Bars are for people who want natural ingredients like rolled oats, soybeans, and organic soy flour.

Exhibit 8.3

Lifestyle Segmentation of the Snack-Food Market

	Nutritional Snackers	Weight Watchers	Guilty Snackers	Party Snackers	Indiscriminate Snackers	Economical Snackers
% of Snackers	22 %	14 %	9 %	15 %	15 %	18 %
Lifestyle Characteristics	Self-assured, controlled	Outdoorsy, influential, adventuresome	Highly anxious, isolated	Sociable	Hedonistic	Self-assured, price-oriented
Benefits Sought	Nutritious, without artificial ingredients, natural	Low in calories, quick energy	Low in calories, good tasting	Good to serve guests, goes well with beverages	Good tasting, satisfies hunger	Low in price, best value
Consumption Level of Snacks	Light	Light	Heavy	Average	Heavy	Average
Type of Snacks Usually Eaten	Fruits, vegetables, cheese	Yogurt, vegetables	Yogurt, cookies, crackers, candy	Nuts, potato chips, crackers, pretzels	Candy, ice cream, cookies, potato chips, pretzels, popcorn	No specific products
Demographics	Better educated, have young children	Young, single	Younger or older, female, lower socioeconomic status	Middle-aged, no urban	Teenager	Have large family, better educated

USAGE-RATE SEGMENTATION

usage-rate segmentation
Dividing a market by the amount of product bought or consumed.

80/20 principle
A principle holding that 20 percent of all customers generate 80 percent of the demand.

Usage-rate segmentation divides a market by the amount of product bought or consumed. Categories vary by product, but they are likely to include some combination of the following: former users, potential users, first-time users, light or irregular users, medium users, and heavy users. Segmenting by usage rate enables marketers to target heavy users or to develop multiple marketing mixes aimed at different segments. Because heavy users often account for a sizable portion of all product sales, some marketers focus on the heavy-user segment.

The 80/20 principle holds that 20 percent of all customers generate 80 percent of the demand. Although the percentages are rarely exact, the general idea often holds true. For example, in the fast food industry, the heavy user accounts for only one of five fast food patrons, but makes about 60 percent of all visits to fast food restaurants. Fewer than 10 percent of the subscribers to Time Warner's cable unit consume more than 75 percent of its bandwidth.[39] The needs of heavy users differ from those of other usage-rate groups. They require product and service selection and a variety of types of information, as well as an emotional attachment to the product category. Individuals in heavy-user groups spend four to fourteen times as much as light users.[40]

Frequency/loyalty programs, like airlines' frequent flyer programs, are designed to develop customers into heavy users. Many supermarkets and other retailers have also designed loyalty programs that reward the heavy-user segment with deals available only to them, including in-store coupon dispensing systems, loyalty card programs, and special price deals on selected merchandise.

REVIEW LEARNING OUTCOME

LO4 Describe the bases commonly used to segment consumer markets

Geography	Demographics	Psychographics	Benefits	Usage Rate
• Region • Market size • Market density • Climate	• Age • Gender • Income • Race/ethnicity • Family life cycle	• Personality • Motives • Lifestyle • Geodemographics	• Benefits sought	• Former • Potential • 1st time • Light or irregular • Medium • Heavy

LO5

Bases for Segmenting Business Markets

The business market consists of four broad segments: producers, resellers, government, and institutions. (For a detailed discussion of the characteristics of these segments, see Chapter 7.) Whether marketers focus on only one or on all four of these segments, they are likely to find diversity among potential customers. Thus, further market segmentation offers just as many benefits to business marketers as it does to consumer-product marketers.

COMPANY CHARACTERISTICS

Company characteristics, such as geographic location, type of company, company size, and product use, can be important segmentation variables. Some markets are regional because buyers prefer to purchase from local suppliers, and distant suppliers may have difficulty competing in terms of price and service. Therefore, firms that sell to geographically concentrated industries benefit by locating close to their markets.

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Segmenting by customer type lets business marketers tailor their marketing mixes to the unique needs of particular types of organizations or industries. Many companies find this form of segmentation quite effective. For example, Home Depot, one of the largest do-it-yourself retail businesses in the United States, targets professional repair and remodeling contractors alongside "do-it-yourself" consumers. Procter & Gamble targets business customers by focusing on janitors, fast-food workers, maids, and launderers with products specific to each group's cleaning needs.[41]

Volume of purchase (heavy, moderate, light) is a common basis for business segmentation. Another is the buying organization's size, which may affect its purchasing procedures, the types and quantities of products it needs, and its responses to different marketing mixes. Banks frequently offer different services, lines of credit, and overall attention to commercial customers based on their size.

Many products, especially raw materials like steel, wood, and petroleum, have diverse applications. How customers use a product may influence the amount they buy, their buying criteria, and their selection of vendors. For example, a producer of springs may have customers who use the product in applications as diverse as machine tools, bicycles, surgical devices, office equipment, telephones, and missile systems.

satisficers
Business customers who place an order with the first familiar supplier to satisfy product and delivery requirements.

optimizers
Business customers who consider numerous suppliers, both familiar and unfamiliar, solicit bids, and study all proposals carefully before selecting one.

BUYING PROCESSES

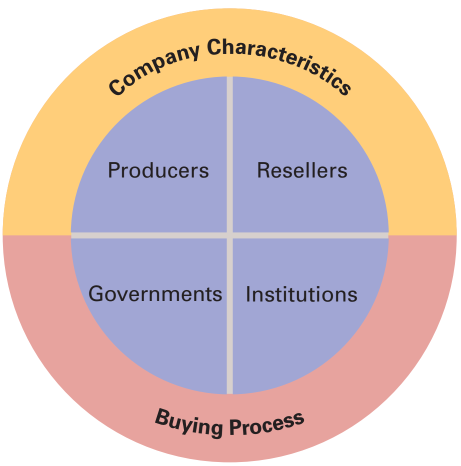
Many business marketers find it helpful to segment customers and prospective customers on the basis of how they buy. For example, companies can segment some business markets by ranking key purchasing criteria, including price, quality, technical support, and service. Atlas Corporation developed a great position in the industrial door market by providing customized products in just 4 weeks, far faster than the industry average of 12 to 15 weeks. Atlas's primary market is companies with an immediate need for customized doors.

The purchasing strategies of buyers may provide useful segments. Two purchasing profiles that have been identified are satisficers and optimizers. Satisficers contact familiar suppliers and place the order with the first one to satisfy product and delivery requirements. Optimizers consider numerous suppliers (both familiar and unfamiliar), solicit bids, and study all proposals carefully before selecting one.

The personal characteristics of the buyers themselves (their demographic characteristics, decision style, tolerance for risk, confidence level, job responsibilities, etc.) influence their buying behavior and thus offer a viable basis for segmenting some business markets. IBM computer buyers, for example, were characterized as being more risk averse than buyers of less expensive computers that perform essentially the same functions. In advertising, therefore, IBM stressed its reputation for high quality and reliability.

REVIEW LEARNING OUTCOME

LO5 Describe the bases for segmenting business markets



LO6 Steps in Segmenting a Market

The purpose of market segmentation, in both consumer and business markets, is to identify marketing opportunities.

1. *Select a market or product category for study*: Define the overall market or product category to be studied. It may be a market in which the firm already competes, a new but related market or product category, or a totally new one. For instance,

Anheuser-Busch closely examined the beer market before introducing Michelob Light and Bud Light. Anheuser-Busch also carefully studied the salty-snack market before introducing the Eagle brand.

2. *Choose a basis or bases for segmenting the market*: This step requires managerial insight, creativity, and market knowledge. There are no scientific procedures for selecting segmentation variables. However, a successful segmentation scheme must produce segments that meet the four basic criteria discussed earlier in this chapter.
3. *Select segmentation descriptors*: After choosing one or more bases, the marketer must select the segmentation descriptors. Descriptors identify the specific segmentation variables to use. For example, if a company selects demographics as a basis of segmentation, it may use age, occupation, and income as descriptors. A company that chooses usage segmentation needs to decide whether to go after heavy users, nonusers, or light users.
4. *Profile and analyze segments*: A profile should include the segments' size, expected growth, purchase frequency, current brand usage, brand loyalty, and long-term sales and profit potential. This information can be used to rank potential market segments by profit opportunity, risk, consistency with organizational mission and objectives, and other key factors.
5. *Select target markets*: Selecting target markets is not a part of but a natural outcome of the segmentation process. It is a major decision that influences and often directly determines the firm's marketing mix. This topic is examined in greater detail later in this chapter.
6. *Design, implement, and maintain appropriate marketing mixes*: The marketing mix has been described as product, place (distribution), promotion, and pricing strategies intended to bring about mutually satisfying exchange relationships with target markets. Chapters 10 through 19 explore these topics in detail.

Markets are dynamic, so it is important that companies proactively monitor their segmentation strategies over time. Often, once customers or prospects have been assigned to a segment, marketers think their task is done. Once customers are assigned to an age segment, for example, they stay there until they reach the next age bracket or category, which could be ten years in the future. Thus, segmentation classifications are static, but customers and prospects are changing. Dynamic segmentation approaches adjust to fit the changes that occur in customers' lives. Abercrombie and Fitch, an apparel store that targets teens opened Ruehl

REVIEW LEARNING OUTCOME

LO 6 List the steps involved in segmenting markets

1 Select a market or product category for study. → **2** Choose a basis or bases for segmenting the market. → **3** Select segmentation descriptors. → **4** Profile and analyze segments. → **5** Select target markets. → **6** Design, implement, and maintain appropriate marketing mixes.

Note that steps 5 and 6 are actually marketing activities that follow market segmentation (steps 1 through 4).

another store, No. 925, to cater to 20-35 year olds; Aeropostale owns Jimmy'Z, which stocks clothing for 18-25 year olds at higher prices than those at its flagship stores for teens; and Pacific Sunwear has a high-end footwear store for young adults called One Thousand Steps.[42]

LO7

Strategies for Selecting Target Markets

target market
A group of people or organizations for which an organization designs, implements, and maintains a marketing mix intended to meet the needs of that group, resulting in mutually satisfying exchanges.

undifferentiated targeting strategy
A marketing approach that views the market as one big market with no individual segments and thus uses a single marketing mix.

So far this chapter has focused on the market segmentation process, which is only the first step in deciding whom to approach about buying a product. The next task is to choose one or more target markets. A target market is a group of people or organizations for which an organization designs, implements, and maintains a marketing mix intended to meet the needs of that group, resulting in mutually satisfying exchanges. Because most markets will include customers with different characteristics, lifestyles, backgrounds, and income levels, it is unlikely that a single marketing mix will attract all segments of the market. Thus, if a marketer wishes to appeal to more than one segment of the market, it must develop different marketing mixes. For example, Buick targets people in their sixties with the Lucerne sedan, a luxury car with a V8 engine and OnStar service and targets younger, Generation Y customers with the Enclave, a crossover SUV.[43] The three general strategies for selecting target markets—undifferentiated, concentrated, and multisegment targeting—are illustrated in Exhibit 8.4. Exhibit 8.5 illustrates the advantages and disadvantages of each targeting strategy.

UNDIFFERENTIATED TARGETING

A firm using an undifferentiated targeting strategy essentially adopts a mass-market philosophy, viewing the market as one big market with no individual segments. The firm uses one marketing mix for the entire market. A firm that adopts an undifferentiated targeting strategy assumes that individual customers have similar needs that can be met with a common marketing mix.

The first firm in an industry sometimes uses an undifferentiated targeting strategy. With no competition, the firm may not need to tailor marketing mixes to the preferences of market segments. Henry Ford's famous comment about the Model T is a classic example of an undifferentiated targeting strategy: "They can

Exhibit 8.4
Three Strategies for Selecting Target Markets

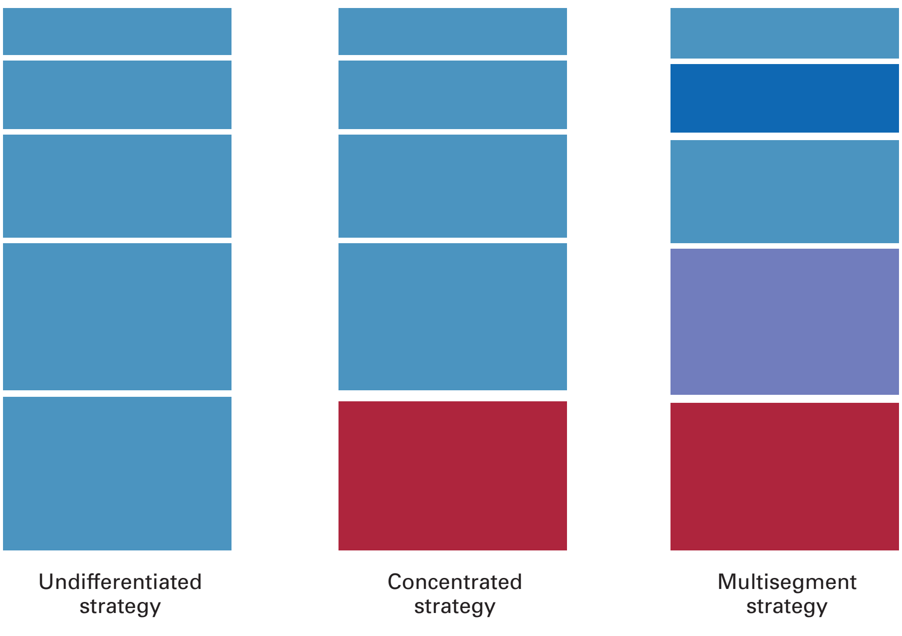


Exhibit 8.5

Advantages and Disadvantages of Target Marketing Strategies

Targeting Strategy	Advantages	Disadvantages
Undifferentiated Targeting	• Potential savings on production/marketing costs • Company more susceptible to competition	• Unimaginative product offerings
Concentrated Targeting	• Concentration of resources • Can better meet the needs of a narrowly defined segment • Allows some small firms to better compete with larger firms • Strong positioning	• Segments too small, or changing • Large competitors may more effectively market to niche segment
Multisegment Targeting	• Greater financial success • Economies of scale in producing/marketing	• High costs • Cannibalization

have their car in any color they want, as long as it's black." At one time, Coca-Cola used this strategy with a single product in a single size of its familiar green bottle. Marketers of commodity products, such as flour and sugar, also tend to use undifferentiated targeting strategies.

One advantage of undifferentiated marketing is the potential for saving on production and marketing. Because only one item is produced, the firm should be able to achieve economies of mass production. Also, marketing costs may be lower when there is only one product to promote and a single channel of distribution. Too often, however, an undifferentiated strategy emerges by default, rather than by design, when a firm fails to consider the advantages of a segmented approach. The result is often sterile, unimaginative product offerings that don't really appeal to anyone.

Another problem associated with undifferentiated targeting is that it makes the company more susceptible to competitive inroads. Hershey lost a big share of the candy market to Mars and other candy companies before it changed to a multisegment targeting strategy. Coca-Cola lost its position as the leading seller of cola drinks in supermarkets to Pepsi-Cola in the late 1950s when Pepsi began offering multiple container sizes.

You might think a firm producing a standard product like toilet tissue would adopt an undifferentiated strategy. However, this market has industrial segments and consumer segments. Industrial buyers want an economical, single-ply product sold in boxes of a hundred rolls. The consumer market demands a more versatile product in smaller quantities. Within the consumer market, the product is differentiated with designer print or no print, cushioned or noncushioned, and economy priced or luxury priced. Fort Howard Corporation, the market share leader in industrial toilet paper, does not even sell to the consumer market.

Undifferentiated marketing can succeed in certain situations, though. A grocery store in a small, isolated town may define all local residents as its target market. It may offer one marketing mix and generally satisfy everyone in town. This strategy is not likely to be as effective if there are three or four grocery stores in the town.

concentrated targeting strategy
A strategy used to select one segment of a market for targeting marketing efforts.

niche
One segment of a market.

CONCENTRATED TARGETING

With a concentrated targeting strategy, a firm selects a market niche (one segment of a market) for targeting its marketing efforts. Because the firm appeals to a single segment, it can concentrate on understanding the needs, motives, and satisfactions of that segment's members and on developing and maintaining a highly specialized marketing mix. Some firms find that concentrating resources and meeting the needs of a narrowly defined market segment is more profitable than spreading resources over several different segments.

For example, Starbucks became successful by focusing on consumers who want gourmet coffee products. America Online (AOL) became a leading Internet provider by targeting Internet newcomers. By making the Internet interface easy to use, AOL attracted millions of people who might not otherwise subscribe to an online service. Watch makers Patek Philippe, Rolex, and Breguet, which sell watches priced at $200,000 and above definitely pursue a concentrated targeting strategy. So does AARP if you consider people over 50 years old to be a single market segment of the overall population.

Small firms often adopt a concentrated targeting strategy to compete effectively with much larger firms. For example, Enterprise Rent-A-Car rose to the top of the car rental industry by catering to people with cars in for repairs. Then it expanded into the airport rental market. A number of new banks, including Solara National Bank in Denver, Colorado, have opened to serve Spanish-speaking customers. Solara caters to this market's needs better than large financial institutions by providing nontraditional services like financial literacy, mentoring, and hand holding for customers as they transition from a cash economy to using bank products and services.[44] New cell phone services cater to small consumer niches. For example, Long Island Ducks targets fans of the minor league baseball team, Yoga Phone is for people who do yoga, and Mobile Swami provides daily meditation tips.[45] Some firms, on the other hand, use a concentrated strategy to establish a strong position in a desirable market segment. Porsche, for instance, targets an upscale automobile market through "class appeal, not mass appeal."

multisegment targeting strategy
A strategy that chooses two or more well-defined market segments and develops a distinct marketing mix for each.

IMAGE COURTESY OF THE ADVERTISING ARCHIVES

Brands with a multisegment targeting approach develop marketing mixes for more than one distinct market segment. In this advertisement, Ralph Lauren displays the versatility of its brand by pointing out that it makes clothing for children as well as for teenagers and young adults.

Concentrated targeting violates the old adage "Don't put all your eggs in one basket." If the chosen segment is too small or if it shrinks due to environmental changes, the firm may suffer. For instance, OshKosh B'Gosh, Inc., was highly successful selling children's wear in the 1980s. It was so successful, however, that the children's line came to define OshKosh's image to the extent that the company couldn't sell clothes to anyone else. It abandoned attempts to market older children's clothing, women's casual clothes, and maternity wear and, recognizing that it was in the children's wear business, OshKosh expanded into products such as kids' shoes, children's eyewear, and plush toys.

A concentrated strategy can also be disastrous for a firm that is unsuccessful in its narrowly defined target market. Before Procter & Gamble introduced Head and Shoulders shampoo, several small firms were already selling antidandruff shampoos. Head and Shoulders was introduced with a large promotional campaign, and the new brand captured over half the market immediately. Within a year, several of the firms that had been concentrating on this market segment went out of business.

MULTISEGMENT TARGETING

A firm that chooses to serve two or more well-defined market segments and develops a distinct marketing mix for each has a multisegment targeting strategy. Many universities offer full-time (day) MBA programs, professional (evening) programs, and executive (weekend) programs, each targeted at a distinctly different market segment. Many programs target mothers returning to the workplace. Cosmetics companies try to increase sales and market share by targeting multiple age and ethnic groups. Maybelline and Cover Girl, for example, market different lines to teenagers, young adult women, older women, and African American women. CitiCard offers its Upromise Card to those who want to save money for college, its Platinum Select Card to those who want no annual fee and a competitive interest rate, its Diamond Preferred Rewards Card to customers who want to earn free rewards like travel and brand-name merchandise, and its Citi AAdvantage Card to those who want to earn American Airlines Advantage frequent flyer miles to redeem for travel. Many credit-card companies have programs specifically designed for tweens, teens, and college students.[46] Wal-Mart historically followed a concentrated strategy that targeted lower income segments. Recently, however, the company segmented its customers into three core groups based on the type of value they seek at the stores. "Brand Aspirationals" are low income customers who want brand names like KitchenAid, "Price-Sensitive Affluents" are wealthier shoppers who love deals, and "Value-Price Shoppers" like low prices and can't afford much more.[47]

Sometimes organizations use different promotional appeals, rather than completely different marketing mixes, as the basis for a multisegment strategy. Beer marketers such as Adolph Coors and Anheuser-Busch advertise and promote special events targeted toward African American, Hispanic American, and Asian American market segments. The beverages and containers, however, do not differ by ethnic market segment.

Multisegment targeting is used for stores and shopping formats, not just brands. In the past, Best Buy treated all its customers, identically according to CEO Bradbury Anderson. But its customers aren't the same. The company has identified five types of customers and given each type a name: "Jill," a busy suburban mom; "Buzz," a focused, active younger male; "Ray," a family man who likes his technology practical; "BB4B" (short for Best Buy for Business), a small employer; and "Barry," an affluent professional male who's likely to drop tens of thousands of dollars on a home theater system.[48]

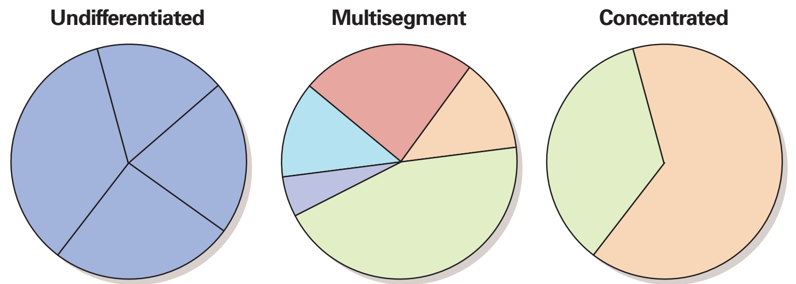
Gap, Inc., takes a different approach. It uses family and individual branding for its alternative format outlets targeting different market segments. Stores operating under the family brand include Gap, Gapkids, babyGap, GapBody, and Gap Outlet. Individual brands other than Gap include Banana Republic and Old Navy. Multisegment targeting offers many potential benefits to firms, including greater sales volume, higher profits, larger market share, and economies of scale in manufacturing and marketing. Yet it may also involve greater product design, production, promotion, inventory, marketing research, and management costs. Before deciding to use this strategy, firms should compare the benefits and costs of multisegment targeting to those of undifferentiated and concentrated targeting.

cannibalization
A situation that occurs when sales of a new product cut into sales of a firm's existing products.

Another potential cost of multisegment targeting is cannibalization, which occurs when sales of a new product cut into sales of a firm's existing products. In many cases, however, companies prefer to steal sales from their own brands rather than lose sales to a competitor. Also, in today's fast-paced world of Internet business, some companies are willing to cannibalize existing business to build new business. Code Red, part of PepsiCo's multisegmentation approach, got a quarter of its volume from Mountain Dew drinkers.[49]

REVIEW LEARNING OUTCOME

LO7 Discuss alternative strategies for selecting target markets



LO8

One-to-One Marketing

one-to-one marketing
An individualized marketing method that utilizes customer information to build long-term, personalized, and profitable relationships with each customer.

Most businesses today use a mass-marketing approach designed to increase *market share* by selling their products to the greatest number of people. For many businesses, however, it is more efficient and profitable to use one-to-one marketing to increase *share of customer*—in other words, to sell more products to each customer. One-to-one marketing is an individualized marketing method that utilizes customer information to build long-term, personalized, and profitable relationships with each customer. The goal is to reduce costs through customer retention and increase revenue through customer loyalty. For example, Tesco, the British supermarket chain, sends mailings to 11 million households each quarter —but it produces 4 million different versions, tailored to the interests of its diverse customer base.[50]

The difference between one-to-one marketing and the traditional mass-marketing approach can be compared to that between a rifle and a shotgun. If you have good aim, a rifle is the more efficient weapon to use. A shotgun, on the other hand, increases your odds of hitting the target when it is more difficult to focus. Instead of scattering messages far and wide across the spectrum of mass media (the shotgun approach), one-to-one marketers look for opportunities to communicate with each individual customer (the rifle approach).

Anya Hindmarch, one of Britain's leading handbag and accessory designers, invites her customers to participate in the creation of their handbags by providing a personal photograph that she expertly transposes onto one of her beautifully designed bags. Customers may also participate in the design process in other ways to create a unique, one-of-a-kind, customer-designed handbag.[51]

Land's End also engages in one-to-one marketing. On Lands' End's Web site, customers spend 20 minutes answering a series of questions. Their sizing information is saved to simplify reordering. Customers who customize have been found to be more loyal.

Several factors suggest that personalized communications and product customization will continue expanding as more and more companies understand why and how their customers make and execute purchase decisions. At least four trends will support the ongoing growth of one-to-one marketing.

First, the one-size-fits-all marketing of yesteryear is no longer relevant. Consumers do not want to be treated like the masses; they want to be treated as the individuals they are, with their own unique sets of needs and wants. By its personalized nature, one-to-one marketing can fulfill this desire.

© REUTERS NEWMEDIA INC./CORBIS

How serious are companies about giving customers individualized attention? Levi Strauss has a shrink tub in its San Francisco megastore so that customers can shrink their jeans to fit. After the shrink tub, they pass through the human dryer before leaving the store.

Second, more direct and personal marketing efforts will continue growing to meet the needs of consumers who no longer have the time to spend shopping and making purchase decisions. With the personal and targeted nature of one-to-one marketing, consumers can spend less time making purchase decisions and more time doing the things that are important.

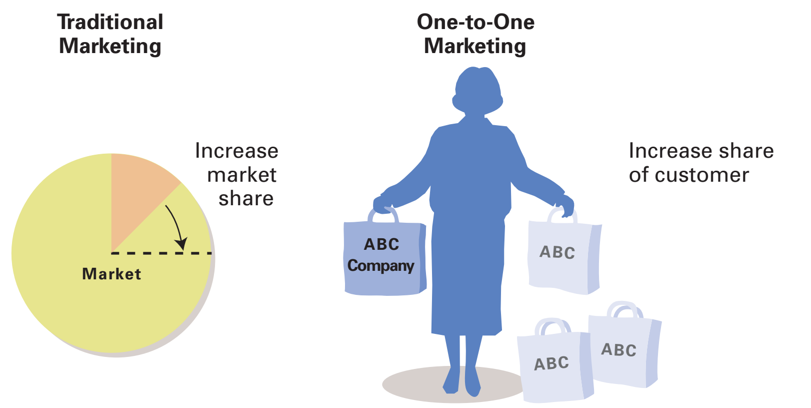
Third, consumers will be loyal only to those companies and brands that earn their loyalty and reinforce it at every purchase occasion. One-to-one marketing techniques focus on finding a firm's best customers, rewarding them for their loyalty, and thanking them for their business.

Fourth, mass-media approaches will decline as advances in market research and database technology enable marketers to collect detailed information on their customers, not just the approximation offered by demographics but the specific names and addresses. New technology offers one-to-one marketers a more cost-effective way to reach customers and enables businesses to personalize their messages. For example, MyYahoo.com greets each user by name and offers information in which the user has expressed interest. Similarly, RedEnvelope.com helps customers keep track of special occasions and offers personalized gift recommendations. Dell, Inc. and Starbucks are well-known examples of one-to-one product customization, but more and more companies are making it possible for customers to customize their purchases. With the help of database technology, one-to-one marketers can track their customers as individuals, even if they number in the millions.

One-to-one marketing is a huge commitment and often requires a 180-degree turnaround for marketers who spent the last half of the twentieth century developing and implementing mass-marketing efforts. Although mass marketing will probably continue to be used, especially to create brand awareness or to remind consumers of a product, the advantages of one-to-one marketing cannot be ignored.

REVIEW LEARNING OUTCOME

LO8 Explain one-to-one marketing



LO9 Positioning

positioning Developing a specific marketing mix to influence potential customers' overall perception of a brand, product line, or organization in general.

position The place a product, brand, or group of products occupies in consumers' minds relative to competing offerings.

product differentiation A positioning strategy that some firms use to distinguish their products from those of competitors.

The development of any marketing mix depends on positioning, a process that influences potential customers' overall perception of a brand, product line, or organization in general. Position is the place a product, brand, or group of products occupies in consumers' minds relative to competing offerings. Consumer goods marketers are particularly concerned with positioning. Procter & Gamble, for example, markets 11 different laundry detergents, each with a unique position, as illustrated in Exhibit 8.6.

Positioning assumes that consumers compare products on the basis of important features. Marketing efforts that emphasize irrelevant features are therefore likely to misfire. For example, Crystal Pepsi and a clear version of Coca-Cola's Tab failed because consumers perceived the "clear" positioning as more of a marketing gimmick than a benefit.

Effective positioning requires assessing the positions occupied by competing products, determining the important dimensions underlying these positions, and choosing a position in the market where the organization's marketing efforts will have the greatest impact. For example, AT&T's wireless company has positioned itself as mobility-centric, offering seamless mobility for customers with on-the-go lifestyles.[52] Callaway Golf positions its new line of clubs and balls as innovative and technologically superior, using the tag line "A better game by design."[53] As the previous examples illustrate, product differentiation is a positioning strategy that many firms use to distinguish their products from those of competitors. The distinctions can be either real or perceived. Tandem Computer designed machines with two central processing units and two memories for computer systems that can never afford to be down or lose their databases (for example, an airline reservation system). In this case, Tandem used product differentiation to create a product with

Exhibit 8.6

Positioning of Procter & Gamble Detergents

Brand	Positioning	Market Share
Tide	Tough, powerful cleaning	31.1 percent
Cheer	Tough cleaning and color protection	8.2 percent
Bold	Detergent plus fabric softener	2.9 percent
Gain	Sunshine scent and odor-removing formula	2.6 percent
Era	Stain treatment and stain removal	2.2 percent
Dash	Value brand	1.8 percent
Oxide	Bleach-boosted formula, whitening	1.4 percent
Solo	Detergent and fabric softener in liquid form	1.2 percent
Dreft	Outstanding cleaning for baby clothes, safe for tender skin	1.0 percent
Ivory Snow	Fabric and skin safety on baby clothes and fine washables	0.7 percent
Ariel	Tough cleaner, aimed at Hispanic market	0.1 percent

very real advantages for the target market. However, many everyday products, including bleaches, aspirin, unleaded regular gasoline, and some soaps, are differentiated by such trivial means as brand names, packaging, color, smell, or "secret" additives. The marketer attempts to convince consumers that a particular brand is distinctive and that they should demand it over competing brands.

Some firms, instead of using product differentiation, position their products as being similar to competing products or brands. Artificial sweeteners advertised as tasting like sugar are one example.

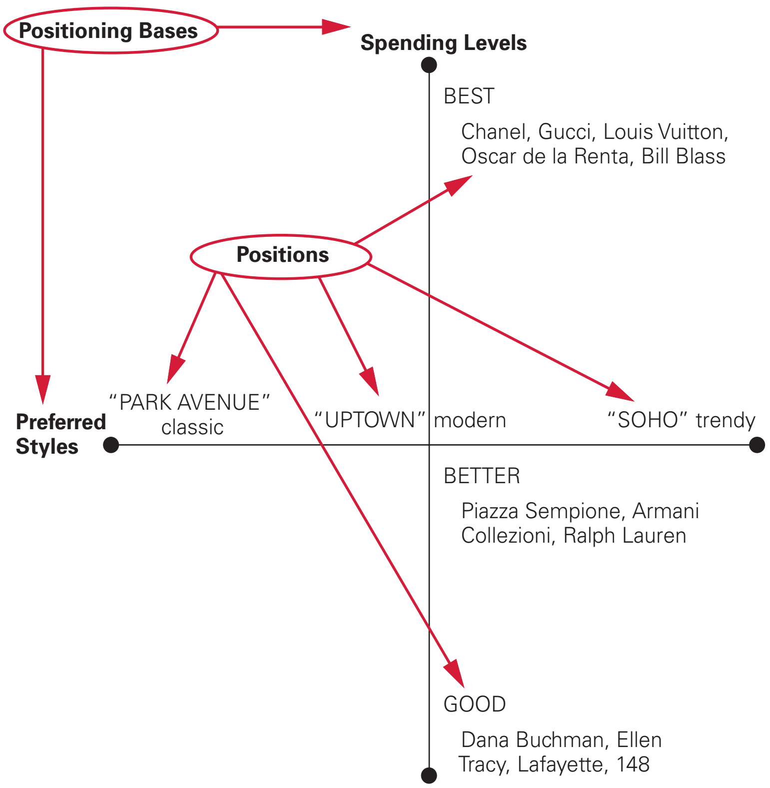
PERCEPTUAL MAPPING

perceptual mapping
A means of displaying or graphing, in two or more dimensions, the location of products, brands, or groups of products in customers' minds.

Perceptual mapping is a means of displaying or graphing, in two or more dimensions, the location of products, brands, or groups of products in customers' minds. For example, Saks Inc. stumbled in sales when it tried to attract a younger core customer. To recover, Saks invested in research to determine its core customers in its 54 stores across the country. The perceptual map in Exhibit 8.7 shows how Saks Inc. uses customer demographics; for instance, a matrix charts the best mix of clothes and accessories to stock in each store.

Exhibit 8.7

Perceptual Map and Positioning Strategy for Saks' Department Stores



SOURCE: Based on Vanessa O'Connell, "Park Avenue Classic or Soho Trendy?" *The Wall Street Journal*, April 20, 2007, B1.

POSITIONING BASES

Firms use a variety of bases for positioning, including the following:

- *Attribute:* A product is associated with an attribute, product feature, or customer benefit. Kleenex has designed a tissue that contains germ-killing substances in an effort to differentiate its product from competing tissues.[54]
- *Price and quality:* This positioning base may stress high price as a signal of quality or emphasize low price as an indication of value. Neiman Marcus uses the high-price strategy; Wal-Mart follows the low-price and value strategy. The mass merchandiser Target developed an interesting position based on price and quality. It is an "upscale discounter," sticking to low prices but offering higher quality and design than most discount chains.
- *Use or application:* Stressing uses or applications can be an effective means of positioning a product with buyers. Kahlúa liqueur used advertising to point out 228 ways to consume the product.

© PR NEWSFOTO/KAY JEWELERS

Diamond companies and jewelers are working to "reposition" the diamond ring so that women will not think of them solely as a symbol of engagement and marriage. In new ad campaigns, women are encouraged to buy a "right-hand" ring as an expression of individuality.

- *Product user:* This positioning base focuses on a personality or type of user. Zale Corporation has several jewelry store concepts, each positioned to a different user. The Zales stores cater to middle-of-the-road consumers with traditional styles. Its Gordon's stores appeal to a slightly older clientele with a contemporary look. Guild is positioned for affluent 50-plus consumers.
- *Product class:* The objective here is to position the product as being associated with a particular category of products; for example, positioning a margarine brand with butter. Alternatively, products can be disassociated with a category. Del Monte has introduced Fruit Chillers, a shelf-stable sorbet that consumers freeze themselves when they're ready to eat it. Fruit Chillers are sold next to single serve fruit cups, positioned as fruit rather than as a frozen dessert.[55]
- *Competitor:* Positioning against competitors is part of any positioning strategy. The original Avis rental car positioning as number 2 compared to Hertz exemplifies positioning against specific competitors.

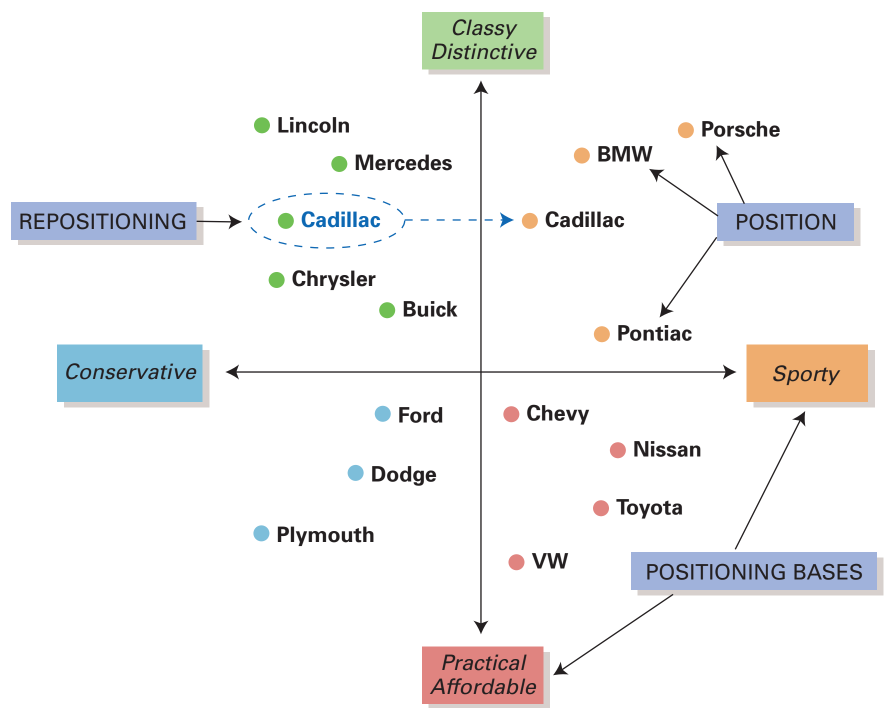
repositioning
Changing consumers' perceptions of a brand in relation to competing brands.

- *Emotion:* Positioning using emotion focuses on how the product makes customers feel. A number of companies use this approach. For example, Nike's "Just Do It" campaign didn't tell consumers what "it" was, but most got the emotional message of achievement and courage. Budweiser's advertising featuring talking frogs and lizards emphasized fun. Sears drew on the nostalgia of its brand name by remodeling a store outside Atlanta to resemble its stores of the past. The move highlighted Sears' heritage, and its legacy as America's store.[56]

REVIEW LEARNING OUTCOME

LO9 Explain how and why firms implement positioning strategies and how product differentiation plays a role

Each car occupies a position in consumers' minds.
Cars can be positioned according to attribute (sporty, conservative, etc.), to price/quality (affordable, classy, etc.) or other bases.
Cadillac has repositioned itself as a car for younger drivers with edgier ads.



REPOSITIONING

Sometimes products or companies are repositioned in order to sustain growth in slow markets or to correct positioning mistakes. **Repositioning** is changing consumers' perceptions of a brand in relation to competing brands. For example, Procter & Gamble increased its baby-care business in the early 2000s when they changed Pampers' position from emphasizing dryness to focusing on helping Mom with her baby's development. P&G also repositioned Olay from being a pink moisturizing liquid to helping women look better and feel better as they age.[57] One entire industry that needs to think about repositioning is the supermarket industry. For over a decade, Wal-Mart has expanded in both rural and metro areas. The results have generally been devastating to competitors, especially independent grocers. Consulting firm Retail Forward predicts that two supermarkets will go out of business for every Wal-Mart Supercenter that opens in the United States. The Strategic Resource Group adds that 27 leading national and regional supermarket operators have either gone bankrupt or liquidated since Wal-Mart went national with Supercenters.[58] So what should competitors do? Wal-Mart owns the low price position. Successful competitors will have to establish viable alternative positions.

H-E-B stores in Hispanic areas in Texas tailor their product mix to appeal to this market segment. H-E-B also opened Asian markets in some stores. Its Central Market format is upscale with unique products and high-quality perishables. Research shows that over half of all families with incomes between $50,000 and $100,000 are willing to pay more for high-quality items in a more pleasant shopping environment.[59] Safeway is trying to avoid Wal-Mart by repositioning itself as upscale and converting half its stores to "Lifestyle" markets with wood floors, on-site bakeries, and high-end private label brands.[60]

It is too early to tell which, if any, of these repositioning strategies will succeed. Clearly, though, competing head-on with Wal-Mart is a bad idea.

$15 billion < amount marketers spend yearly advertising to young children

television commercials viewed by children each year > **40,000**

20 billion < tweens in the U.S.

percentage of U.S. online purchases made by teenagers > **3**

percentage of consumer purchases made or influenced by women > **80**

$86 billion < single adults living in the U.S.

percentage of people who say cars make them feel powerful > **25**

starting price of a Breuguet watch > **$200,000**

5 < customer types identified by Best Buy

laundry detergents marketed by Procter & Gamble > **11**

Review and Applications

LO 1

Describe the characteristics of markets and market segments. A market is composed of individuals or organizations with the ability and willingness to make purchases to fulfill their needs or wants. A market segment is a group of individuals or organizations with similar product needs as a result of one or more common characteristics.

1.1 Mercedes-Benz is thinking about advertising its cars to college students. Do you think that college students are a viable potential market for Mercedes? Why or why not?

ONLINE

1.2 Go to the Web site **http://www.careermag.com.** How are visitors to the site segmented when seeking relevant job openings? Report your results.

LO 2

Explain the importance of market segmentation. Before the 1960s, few businesses targeted specific market segments. Today, segmentation is a crucial marketing strategy for nearly all successful organizations. Market segmentation enables marketers to tailor marketing mixes to meet the needs of particular population segments. Segmentation helps marketers identify consumer needs and preferences, areas of declining demand, and new marketing opportunities.

2.1 Describe market segmentation in terms of the historical evolution of marketing.

LO 3

Discuss criteria for successful market segmentation. Successful market segmentation depends on four basic criteria: (1) a market segment must be substantial and have enough potential customers to be viable; (2) a market segment must be identifiable and measurable; (3) members of a market segment must be accessible to marketing efforts; and (4) a market segment must respond to particular marketing efforts in a way that distinguishes it from other segments.

WRITING

3.1 As a marketing consultant for a chain of hair salons, you have been asked to evaluate the kids' market as a potential segment for the chain to target. Write a memo to your client discussing your evaluation of the kids' segment in terms of the four criteria for successful market segmentation.

LO4

Describe the bases commonly used to segment consumer markets. Five bases are commonly used to segment consumer markets. Geographic segmentation is based on region, size, density, and climate characteristics. Demographic segmentation is based on age, gender, income level, ethnicity, and family life-cycle characteristics. Psychographic segmentation includes personality, motives, and lifestyle characteristics. Benefits sought identifies customers according to the benefits they seek in a product. Finally, usage segmentation divides a market by the amount of product purchased or consumed.

WRITING

4.1 Choose magazine ads for five different consumer products. For each ad, write a description of what you think the demographic characteristics of the targeted market are.

ONLINE

4.2 Investigate how Delta Air Lines (**http://www.delta.com**) uses its Web site to cater to its market segments.

4.3 Is it possible to identify a single market for two distinctly different products? For example, how substantial is the market comprised of consumers who use Apple *and* who drive Volkswagens? Can you think of other product combinations that would interest a single market? (Do not use products that are complementary, like a bike and a bike helmet. Think of products, like the iPod and the car, that are very different.) Complete the following sentences and describe the market for each set of products you pair together.

Consumers of:

Propel fitness water could also be a target market for ________________.

Proactiv Solution skin care products could also be a target market for ________________.

Alienware computers could also be a target market for ________________.

Specialty luggage tags could also be a target market for ________________.

LO5

Describe the bases for segmenting business markets. Business markets can be segmented on two general bases. First, businesses segment markets based on company characteristics, such as customers' geographic location, type of company, company size, and product use. Second, companies may segment customers based on the buying processes those customers use.

5.1 Choose five ads from business publications such as *The Wall Street Journal*, *Fortune*, and *BusinessWeek*. For each ad, write a description of how you think the company has segmented its business market.

LO6

List the steps involved in segmenting markets. Six steps are involved when segmenting markets: (1) selecting a market or product category for study; (2) choosing a basis or bases for segmenting the market; (3) selecting segmentation descriptors; (4) profiling and evaluating segments; (5) selecting target markets; and (6) designing, implementing, and maintaining appropriate marketing mixes.

WRITING

6.1 Write a letter to the president of your bank suggesting ideas for increasing profits and enhancing customer service by improving segmentation and targeting strategies.

LO7

Discuss alternative strategies for selecting target markets. Marketers select target markets using three different strategies: undifferentiated targeting, concentrated targeting, and multisegment targeting. An undifferentiated targeting strategy assumes that all members of a market have similar needs that can be met with a single marketing mix. A concentrated targeting strategy focuses all marketing efforts on a single market segment. Multisegment targeting is a strategy that uses two or more marketing mixes to target two or more market segments.

7.1 Form a team with two or three other students. Create an idea for a new product. Describe the segment (or segments) you will target with the product and explain why you chose the targeting strategy you did.

7.2 Go to the Web sites of JCPenney, **http://www.jcpenney.com,** and Target, **http://www.target.com.** Compare the presentation of women's fashions. What are the major differences? Which site is more designer focused, and which is more brand focused? Which company's approach do you think will appeal more to the "Holy Grail" target market of 25- to 35-year-old women?

LO8 **Explain one-to-one marketing.** One-to-one marketing is an individualized marketing method that utilizes customer information to build long-term, personalized, and profitable relationships with each customer. Successful one-to-one marketing comes from understanding customers and collaborating with them rather than using them as targets for generic messages. Database technology makes it possible for companies to interact with customers on a personal, one-to-one basis.

8.1 You are the marketing manager for a specialty retailer that sells customized handbags. Write a memo to your boss describing how the company could benefit from one-to-one marketing.

LO9 **Explain how and why firms implement positioning strategies and how product differentiation plays a role.** Positioning is used to influence consumer perceptions of a particular brand, product line, or organization in relation to competitors. The term *position* refers to the place that the offering occupies in consumers' minds. To establish a unique position, many firms use product differentiation, emphasizing the real or perceived differences between competing offerings. Products may be differentiated on the basis of attribute, price and quality, use or application, product user, product class, or competitor.

9.1 Choose a product category (e.g., pick-up trucks), and identify at least three different brands and their respective positioning strategies. How is each position communicated to the target audience?

Key Terms

benefit segmentation	242	market segment	231	product differentiation	251
cannibalization	249	market segmentation	231	psychographic segmentation	241
concentrated targeting strategy	247	multisegment targeting strategy	248	repositioning	253
demographic segmentation	234	niche	247	satisficers	244
80/20 principle	243	one-to-one marketing	250	segmentation bases (variables)	233
family life cycle (FLC)	239	optimizers	244	target market	246
geodemographic segmentation	241	perceptual mapping	252	undifferentiated targeting strategy	246
geographic segmentation	234	position	251	usage-rate segmentation	243
market	231	positioning	251		

Exercises

APPLICATION EXERCISE

How tightly do you fit into a particular market segment? Do you think you can be neatly classified? If you think your purchasing habits make you an enigma to marketers, you may need to think again.[61]

Activities

1. Go to the Claritas Web site (**http://www.claritas.com**) and follow its "You Are Where You Live" link to find out what your ZIP code says about you. The database will generate many cluster descriptions based on your ZIP code. Depending on the functionality of the Web site at

the time you access the database, you may need to reenter your ZIP code multiple times if you want to read all the cluster descriptions.

2. Now pick a product category, like automobiles, athletic shoes, beverages, or health and beauty products. Then think about which products in that category would appeal to each of the clusters generated by your ZIP code search. For example, a car that appeals to a cluster titled "Young Bohemians" may not be the car of choice for the cluster "Pools and Patios." If your search generated only one cluster type, you may wish to enter other ZIP codes for your area of town or for your region.
3. Create a perceptual map for the product you chose. Write a short statement that describes the overall position of each product with an explanation of why you located it where you did on the perceptual map.

ETHICS

ETHICS EXERCISE

Tobacco companies are frequently criticized for targeting potential customers below the legal age to purchase and use their products. Critics cite Joe Camel and the Marlboro man as images meant to make smoking appealing to young people. If tobacco companies are actually following this particular demographic targeting strategy, most would agree that it is unethical if not illegal.

Questions

1. Is marketing tobacco products to younger consumers unethical?
2. Many are beginning to argue that fast-food companies, such as McDonald's and Burger King, are knowingly marketing unhealthy food to consumers. Is it unethical for fast-food companies to market kids' meals to children?
3. What does the AMA Statement of Ethics have to say about marketing unhealthy or harmful products to consumers, particularly children and young adults? Go to the AMA Web site at **http://www.marketingpower.com** to review the statement of ethics. Write a brief paragraph summarizing where the AMA stands on this important issue.

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Case Study: Coke Zero

DO REAL MEN DRINK DIET COKE?

When a couple of marketing managers for Coca-Cola told attorney Elizabeth Finn Johnson that they wanted to sue their Coke Zero colleagues for "taste infringement," she was baffled. She tried to talk them out of it, but they were determined. They argued that Coca-Cola Classic should be protected from the age discrimination it would suffer with the introduction of a newer, younger soft drink that tasted exactly the same as the original. Frustrated, Finn Johnson held up the Coke can and shouted, "It's not a person! Title VII doesn't cover these things!"

What she didn't know was that the marketing managers were actors. Hidden cameras had been planted around the meeting room to capture the reactions of several unsuspecting attorneys who had been asked to consider the case, including an immigration lawyer who was asked if he could get the Coke Zero marketing head deported back to Canada. The short videos were strategically placed on websites like YouTube.com to promote Coke Zero as the hip, new alternative to Diet Coke for men.

The Coca-Cola Company knows it has to be creative if it's going to sell more soda after sales dropped two years in a row in 2005 and 2006. Morgan Stanley analyst Bill Pecoriello explains, "Consumers are becoming ever more health-conscious, and the image of regular carbonated soft drinks is deteriorating rapidly." In an attempt to appeal to consumers concerned with nutrition, Coke introduced Diet Coke Plus in 2007, a sweeter version of Diet Coke fortified with vitamins and minerals. But what they really needed was a way to reach young male consumers, and Diet Coke Plus, marketed with tag lines like "Your Best Friend Just Got Friendlier!" wasn't going to do it.

A few new products appealed to certain male demographics, such as Coca-Cola Blak, a cola with coffee essence created for older, more sophisticated consumers willing to spend more, and Full Throttle Blue Demon, an energy drink with an agave azul flavor (think margaritas) designed to appeal to Hispanic men. However, research showed that there was still a big demographic hole to fill as young men ages 18 to 34 abandoned the Coca-Cola brand altogether. They didn't want all the calories of regular Coke, but they weren't willing to switch to Diet Coke, which has traditionally been marketed to women who want to lose weight.

Katie Bayne, chief marketing officer for Coca-Cola North America, says that the men who weren't put off by the "feminine stigma" of Diet Coke often rejected it anyway because of its aspartame-sweetened aftertaste. "What we were seeing before Zero launched was that more and more younger people were interested in no-calorie beverages but weren't going to sacrifice taste," Bayne said. "So when they got interested in no-calorie, they were like, 'Forget it, I'm not going to Diet Coke.'"

Testing showed that the name "Coke Zero" would be an effective way to sell a low-calorie cola to men without using the word "diet." And advances in artificial sweeteners finally made it possible for Coke to create a product that tasted more like the Real Thing. So expectations were high when Coke Zero was introduced in 2005 with a big marketing push, including a commercial that remade the famous 1971 "Hilltop/I'd Like to Teach the World to Sing" ad—this time with rapper G-Love on a rooftop singing that he'd like to teach the world to "chill." Unfortunately, the commercial didn't catch on, and neither did the product it was selling.

Despite disappointing sales in the U.S., however, Coke Zero was an immediate hit in Australia, selling more than three times the number of cases expected during its first year on the market. In the U.S., the packaging was white and silver, making it difficult for consumers to see the difference between Coke Zero and Diet Coke. In Australia, the bottles and cans were black, making the product stand out on the shelves and look more like the "bloke's Coke" it was intended to be.

The U.S. marketing team took notice and reintroduced Coke Zero with a black and silver label in 2007. Coca-Cola is now investing more money in Coke Zero than any other brand its size, hoping it will someday be a megabrand for the company alongside Coca-Cola Classic and Diet Coke. Chief Marketing Officer Bayne is enthusiastic about the impact it may have on the company. "We do see this as potentially a bit of a white knight. There's huge opportunity to grow here."[62]

Questions

1. Describe the specific type of consumer that the Coca-Cola Company is targeting with each of the following products: Diet Coke, Coke Zero, Diet Coke Plus, Coca-Cola Blak, and Full Throttle Blue Demon. What types of demographic segmentation is each product's marketing most likely to include?
2. Some industry analysts think soft-drink companies should develop products that will bring new customers into the market rather than just creating variants on the old. They warn that products like Coke Zero will cannibalize lost market share from other soft drink categories instead of increasing the number of consumers overall. Which Coca-Cola products are most likely to lose customers to Coke Zero?
3. Why do you think that the hidden-camera videos used to promote Coke Zero were an effective way to reach its target market? Do you think a similar strategy with a viral marketing campaign on the Internet would appeal to the target market for Diet Coke Plus?
4. Do you think Diet Coke could have been repositioned to change consumers' perceptions of it enough to be considered a drink equally appealing to men? Why or why not?

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Company Clips

READYMADE—FOCUS AND SEGMENTATION

ReadyMade markets itself as a magazine catering to GenNest, the group of consumers ages 25 to 35 who are just settling down after college. The young couples that make up this group are buying their first houses and taking on domestic and decorating roles for the first time. They are interested in being stylish while maintaining their own unique personalities. But Ready-Made appeals to a wider variety of readers than just GenNest. The magazine has subscribers in all age groups, from teens looking to spruce up their rooms to retirees seeking for projects to enliven their homes. This diversity offers a unique challenge to ReadyMade as it tries to promote itself to advertisers who need to know what sort of people will be reached through advertisements appearing in the publication.

Questions

1. How does ReadyMade communicate the demographics of its reader base to advertisers who want to see specific statistics that do not easily represent ReadyMade's target market?
2. What sort of segmentation does ReadyMade use when it markets to businesses and investors?
3. What ideas do you have that would help ReadyMade reach out to new subscribers without alienating its loyal base?

Marketing & You Results

A high score indicates that you operate within budget constraints. Living on a budget doesn't necessarily mean that you change your shopping behavior or your price comparison behavior, however. Low scores relate to financial health and a tendency to be brand loyal. After reading Chapter 8, you can see why income and financial situation can be an important segmentation variable!

CHAPTER

9 Decision Support Systems and Marketing Research

Learning Outcomes

- **LO 1** Explain the concept and purpose of a marketing decision support system
- **LO 2** Define marketing research and explain its importance to marketing decision making
- **LO 3** Describe the steps involved in conducting a marketing research project
- **LO 4** Discuss the profound impact of the internet on marketing research
- **LO 5** Discuss the growing importance of scanner-based research
- **LO 6** Explain the concept of competitive intelligence

LO 1

Marketing Decision Support Systems

marketing information
Everyday information about developments in the marketing environment that managers use to prepare and adjust marketing plans.

decision support system (DSS)
An interactive, flexible computerized information system that enables managers to obtain and manipulate information as they are making decisions.

Accurate and timely information is the lifeblood of marketing decision making. Good information can help an organization maximize sales and efficiently use scarce company resources. To prepare and adjust marketing plans, managers need a system for gathering everyday information about developments in the marketing environment—that is, for gathering marketing information. The system most commonly used these days for gathering marketing information is called a *marketing decision support system*.

A marketing decision support system (DSS) is an interactive, flexible computerized information system that enables managers to obtain and manipulate information as they are making decisions. A DSS bypasses the information-processing specialist and gives managers access to useful data at their own desks.

These are the characteristics of a true DSS:

- *Interactive*: Managers give simple instructions and see immediate results. The process is under their direct control; no computer programmer is needed. Managers don't have to wait for scheduled reports.
- *Flexible*: A DSS can sort, regroup, total, average, and manipulate the data in various ways. It will shift gears as the user changes topics, matching information to the problem at hand. For example, the CEO can see highly aggregated figures, and the marketing analyst can view very detailed breakouts.
- *Discovery-oriented*: Managers can probe for trends, isolate problems, and ask "what if" questions.
- *Accessible*: Managers who lack computer skills can easily learn how to use a DSS. Novice users should be able to choose a standard, or default, method of using the system. They can bypass optional features in order to begin working with the basic system immediately and then gradually learn to apply its advanced features.

As a hypothetical example of how a DSS can be used, consider Renee Smith, vice president and manager of new products for Central Corporation. To evaluate sales of a recently introduced product, Renee can "call up" sales by the week, then by the month, breaking them out at her option by, say, customer segments. As she works at her computer, her inquiries can go in several directions, depending on the decision at hand. If her train of thought raises questions about monthly sales last quarter compared to forecasts, she can use her DSS to analyze problems immediately. Renee might see that her new product's sales

Marketing & You

Please note your opinion on each of the following questions.

Using the following scale, enter your opinion.

1	2	3	4	5	6	7
Strongly disagree						Strongly agree

During a marketing project, a marketing manager should have formal or informal processes:

— for continuously collecting information from customers.

— for continuously collecting information about competitors' activities.

— for continuously collecting information about relevant publics other than customers and competitors.

— for continuously reexamining the value of information collected in previous studies.

— for continuously collecting information from external experts, such as consultants.

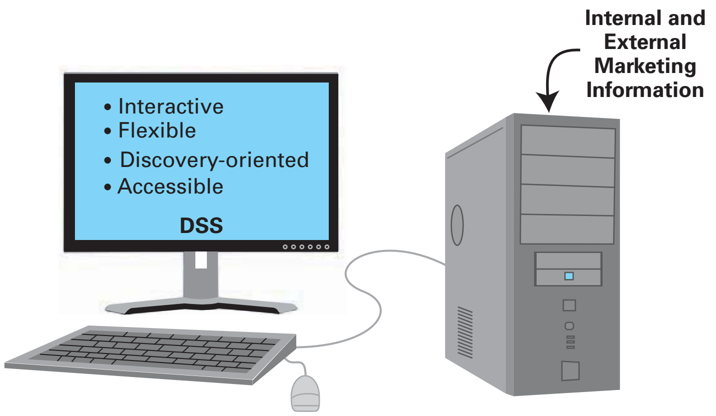
Total your score. Now, read the chapter and find out what your score means at the end.

were significantly below forecasts. Were her forecasts too optimistic? She compares other products' sales to her forecasts and finds that the targets were very accurate. Is something wrong with the product? Is her sales department getting insufficient leads, or is it not putting leads to good use? Thinking a minute about how to examine those questions, she checks ratios of leads converted to sales, product by product. The results disturb her. Only 5 percent of the new product's leads generated orders, compared to the company's 12 percent all-product average. Why? Renee guesses that the sales force is not supporting the new product vigorously enough. Quantitative information from the DSS might provide more evidence to back that suspicion. But, satisfied with her quantitative knowledge to satisfy herself, the VP acts on her intuition and experience and schedules a chat with her sales manager.

Perhaps the fastest-growing use of DSSs is for database marketing, which is the creation of a large computerized file of customers' and potential customers' profiles and purchase patterns. It is usually the key tool for successful one-to-one marketing, which relies on very specific information about a market. Huge databases can raise a number of concerns about the safety and use of personal data.

REVIEW LEARNING OUTCOME

LO 1 Explain the concept and purpose of a marketing decision support system



LO 2 The Role of Marketing Research

database marketing
The creation of a large computerized file of customers' and potential customers' profiles and purchase patterns.

marketing research
The process of planning, collecting, and analyzing data relevant to a marketing decision.

Marketing research is the process of planning, collecting, and analyzing data relevant to a marketing decision. The results of this analysis are then communicated to management. Marketing research plays a key role in the marketing system. It provides decision makers with data on the effectiveness of the current marketing mix and with insights for necessary changes. Furthermore, marketing research is a main data source for both management information systems and DSS. In other words, the findings of a marketing research project become data in a DSS.

Each year over $7 billion is spent on marketing research in the United States. That money is used to study products, advertising, prices, packages, names, logos, services, buying habits, taglines, colors, uses, awareness, familiarity, new concepts, traffic patterns, wants, needs, and politics.

Marketing research has three roles: descriptive, diagnostic, and predictive. Its *descriptive* role includes gathering and presenting factual statements. For example, what is the historic sales trend in the industry? What are consumers' attitudes toward a product and its advertising? Its *diagnostic* role includes explaining data. For instance, how did a change in package design affect sales? Its *predictive* function is to address "what if" questions. For example, how can the researcher use the descriptive and diagnostic research to predict the results of a planned marketing decision?

MANAGEMENT USES OF MARKETING RESEARCH

Marketing research can help managers in several ways. It improves the quality of decision making and helps managers trace problems. Most important, sound marketing research helps managers focus on the paramount importance of keeping existing customers, improves their understanding of the marketplace, and alerts them to marketplace trends.

Marketing research also helps managers gauge the perceived value of their goods and services as well as the level of customer satisfaction. For example, research revealed which brands of plumbing fixtures were traditional in New York City. This helped the Brooklyn Home Depot's store manager Rich Kantor to design his small pilot store to meet the needs of urban communities.

Improving the Quality of Decision Making

Managers can sharpen their decision making by using marketing research to explore the desirability of various marketing alternatives. For example, after the successful launch of its Young & Tender line of bagged spinach, NewStar, a Salinas, California-based produce firm, wondered what it could do for an encore. A line of salad kits featuring spinach in combination with a dressing and/or other ingredients seemed like a natural idea. But instead of introducing a me-too product to the already-crowded salad kit market, the company wanted to add a gourmet twist.

The process began with an idea generation phase, says Christie Hoyer, vice president of product development and evaluation at the National Food Laboratory (NFL). NFL chefs, food technologists, and other culinary arts workers participated in the process. "We did a number of brainstorming sessions, game-playing, and other, more coordinated exercises. From that we came up with numerous flavor concepts for the salads and the sauté mixes."

Next came the first round of consumer testing. At this stage, Hoyer says, NFL wanted to validate its product concepts and also gauge reactions to them. A four-phase process was conducted with male and female consumers ages 21 to 64 who were their family's primary grocery shopper and had positive attitudes towards spinach salad and cooked fresh spinach.

The first phase gathered reactions to the concept of a line of gourmet salad and sauté kits and determined purchase intent for each flavor (based on descriptions of the flavors, not actual tasting). Next the respondents tried the product prototypes, which were rotated so that half of the group tried the sautés first, and half tried the salads first.

© SUSAN VAN ETTEN

Managers can sharpen their decision making by using marketing research to explore various marketing alternatives. Heinz used the results of its marketing research—that is, listening to and watching children using ketchup—to create a new bottle design, name selection, and color for its EZ Squirt ketchup.

The third phase tested packaging. Respondents were taken to a separate area featuring a mock store display of three packaging concepts and asked to rank their preferences for the different graphics. In the fourth phase, the consumers viewed a large copy of the nutritional information for a salad kit and a sauté kit. "Without specifically asking about it, we were interested in their reaction to things such as fat content," Hoyer says.

Since their introduction, the salad and sauté mixes have been a hit with both retailers and consumers. Marketing research paved the way![1]

Since kids eat over 5 billion ounces of ketchup each year, Heinz decided that the heavy users (kids) would have lots to say (via marketing research) about making ketchup fun. Heinz listened and watched children using ketchup, and then used its findings to create a new bottle design, name selection, and color. The true ketchup connoisseurs helped create Heinz EZ Squirt green ketchup.

Tracing Problems

Another way managers use marketing research is to find out why a plan backfired. Was the initial decision incorrect? Did an unforeseen change in the external environment cause the plan to fail? How can the same mistake be avoided in the future?

Keebler introduced Sweet Spots, a shortbread cookies containing huge chocolate drops. They have had acceptable sales and are still on the market, but only because the company used marketing research to overcome several problems. Soon after the cookie's introduction, Keebler increased the box size from 10 ounces at $2.29 to 15 ounces at $3.19. Demand immediately fell. Market research showed that Sweet Spots were now considered more of a luxury than an everyday item. Keebler lowered the price and went back to the 10-ounce box. Even though Sweet Spots originally were aimed at upscale women, the company also tried to appeal to kids. In subsequent research, Keebler found that the package graphics appealed to mothers but not children.

Focusing on the Paramount Importance of Keeping Existing Customers

Customer satisfaction and customer loyalty are inextricably linked. Long-term relationships don't just happen but are grounded in the delivery of service and value by the firm. Customer retention pays big dividends for organizations. Powered by repeat sales and referrals, revenues and market share grow. Costs fall because firms spend less money and energy attempting to replace defectors. Steady customers are easy to serve because they understand the modus operandi and make fewer demands on employees' time. Increased customer retention also drives job satisfaction and pride, leading to higher employee retention. In turn, the knowledge employees acquire as they stay longer increases productivity. A Bain & Co. study estimated that a 5 percent decrease in customer defection can boost profits by 25 to 95 percent.[2] Another study found that the customer retention rate has a major impact on the value of the firm.[3]

Recently, Dunkin' Donuts paid dozens of faithful customers in Phoenix, Chicago, and Charlotte, N.C., $100 a week to buy coffee at Starbucks instead. At the same time, the no-frills coffee chain paid Starbucks customers to make the opposite switch.

When it later debriefed the two groups, Dunkin' says it found them so polarized that company researchers dubbed them "tribes"—each of whom loathed the very things that made the other tribe loyal to their coffee shop. Dunkin' fans viewed Starbucks as pretentious and trendy, while Starbucks loyalists saw Dunkin' as austere and unoriginal.

Bridging some of the divide between Starbucks and Dunkin' Donuts customers—but not too much—is key to Dunkin' Donuts' ambitious plan to expand its largely Eastern coffee chain into a national powerhouse that's as synonymous with coffee as Starbucks.

Dunkin' researchers concluded that what set the two tribes apart wasn't income, but rather an ideal: Dunkin' tribe members wanted to be part of a crowd, while members of the Starbucks tribe wished to stand out as individuals. Dunkin' executives made dozens of decisions, big and small, affecting everything from the espresso machines' locations to the amount of its signature pink and orange color to be retained to where to display fresh-baked goods.

They replaced the square laminate tables, with round imitation-granite tabletops and sleek chairs. Dunkin' covered store walls in espresso brown and dialed down the pink and orange tones. Executives considered, but held off on, installing wireless Internet access because customers "just don't feel it's Dunkin' Donuts," says Joe Scafido, chief creative and innovation officer.[4]

Understanding the Ever-Changing Marketplace

Marketing research also helps managers understand what is going on in the marketplace and take advantage of opportunities. Historically, marketing research has been practiced for as long as marketing has existed. The early Phoenicians carried out market demand studies as they traded in the various ports of the Mediterranean Sea. Marco Polo's diary indicates that he performed marketing research on his way to China. There is even evidence that the Spanish systematically conducted "market surveys" as they explored the New World, and there are examples of marketing research conducted during the Renaissance.

The very first MasterCard "Priceless" commercial showed a father taking his son out to a baseball game. In what would become a famous sequence, the narrator

Exhibit 9.1

The Factors That Make a Sports Fan a Fan

ATHLETE ADMIRATION Based on admiration of talent/ability	PERSONAL INDULGENCE Based on personal selfishness
ATHLETE AFFINITY Based on human relationship with players	NOSTALGIA Based on history and personal memories
ACTIVE APPRECIATION Based on personal participation experience	TEAM OBSESSION Based on loyalty and ardent devotion
BELONGING Based on being identified as part of a tribe	TV PREFERENCE Based on consumption preference
ALL CONSUMING Based on the ability of a property to draw you in	LOVE OF THE SPORT Based on a fundamental love and reverence
GLOATING Based on reveling in the agony of others	TALK & SOCIALIZING Based on social interactions

SOURCE: "What Drives Their Obsession?" *Brandweek* (April 4, 2005), pp. 30-34.

reeled off the cost of a hot dog and a ticket, and then intoned: "real conversation with your 11-year-old son?...Priceless." The ad formed an emotional bond between a sports fan, his son, and, hopefully Mastercard. Octagon, a research and sports marketing company, conducted marketing research to understand the emotional connections fans have with sports—that is, the reason that fans are fans. Octagon uncovered twelve factors they call "passion drivers" that compel fans to follow their favorite sports. These are shown in Exhibit 9.1.

"One of the top drivers for NFL fans [according to the study] was team devotion, so we think we're in the right spot," said Bob Cramer, vp-partner and content integration at MasterCard in Purchase, N.Y.

Cramer said the data support the efficacy of the company's local marketing activities, which include enticements to use Paypass, its contact-less radio frequency product. Fans with cards for rewards programs tied to teams such as the Philadelphia Eagles and Baltimore Ravens can use their cards to speed up transactions in stadiums.[5]

REVIEW LEARNING OUTCOME

LO 2 Define marketing research and explain its importance to marketing decision making

Why marketing research?

- ✓ Improve quality of decision making
- ✓ Trace problems
- ✓ Focus on keeping existing customers
- ✓ Understand changes in marketplace

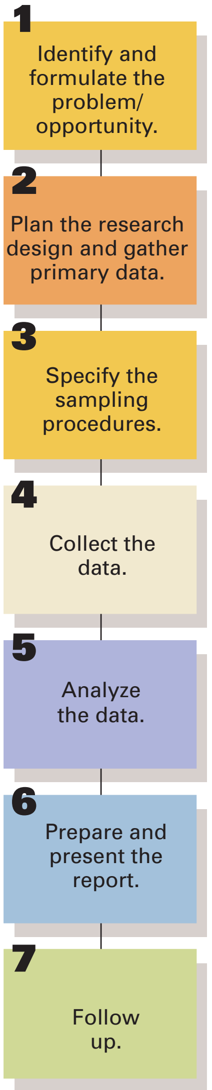
LO 3

Steps in a Marketing Research Project

Virtually all firms that have adopted the marketing concept engage in some marketing research because it offers decision makers many benefits. Some companies spend millions on marketing research; others, particularly smaller firms, conduct informal, limited-scale research studies. For example, when Eurasia restaurant, serving Eurasian cuisine, first opened along Chicago's ritzy Michigan Avenue, it drew novelty seekers. But it turned off the important business lunch crowd, and sales began to decline. The owner surveyed several hundred businesspeople working within a mile of the restaurant. He found that they were confused by Eurasia's concept and wanted more traditional Asian fare at lower prices. In response, the restaurant altered its concept; it hired a Thai chef, revamped the menu, and cut prices. The dining room was soon full again.

Exhibit 9.2

The Marketing Research Process



Whether a research project costs $200 or $2 million, the same general process should be followed. The marketing research process is a scientific approach to decision making that maximizes the chance of getting accurate and meaningful results. Exhibit 9.2 traces the steps: (1) identifying and formulating the problem/opportunity, (2) planning the research design and gathering primary data, (3) specifying the sampling procedures, (4) collecting the data, (5) analyzing the data, (6) preparing and presenting the report, and (7) following up.

The research process begins with the recognition of a marketing problem or opportunity. As changes occur in the firm's external environment, marketing managers are faced with the questions, "Should we change the existing marketing mix?" and, if so, "How?" Marketing research may be used to evaluate product, promotion, distribution, or pricing alternatives.

While the company is largely noted for its well-known line of household lubricants, San Diego-based WD-40 Co. has repositioned one of its product lines as essential bathroom cleaners—the result of a research process.

While sales of the company's six household product brands (including X-14) make up a sizable percentage—more than 31 percent—of its overall portfolio, the X-14 product line lacked cohesion in both packaging design and positioning. Marketed as individual items, rather than as a family of products, they were overshadowed by more popular brands on store shelves.

While the X-14 line is not new, its repositioning helped the $287 million company find the brand's niche. "We previously had products that focused on the bathroom, but there wasn't a unified line in its positioning. We had a line of cleaning products that were not meeting their potential in the marketplace," says Heidi Noorany, Director of Marketing. The marketing research indicated that there was a need for a "bathroom expert" line of products. "We knew we had the positioning and the quality of products within the current line, but we had to communicate it," Noorany adds. That would be translated through the line's more cohesive packaging design characterized by a variety of pinks, oranges and blues as well as several bottle designs.

Consumer research also measured product effectiveness against competitors' products, and found that the X-14 Foaming Bathroom Cleaner scored 4.5 on a scale of 1 to 5, and that its Trigger Bathroom Cleaner had a 91 percent approval rating, placing it above four other competing brands. The research also found that consumers engage in two types of cleaning—weekly deep cleanings and quick daily cleanings. "We saw an opportunity for a bathroom expert line of products," says Noorany. Not only did WD-40 learn how to best reposition the X-14 line, but it garnered insight from the research process to be used in future product development.[6]

The WD-40 story illustrates an important point about problem/opportunity definition. The **marketing research problem** is information oriented. It involves determining what information is needed and how that information can be obtained efficiently and effectively. The **marketing research objective,** then, is to provide insightful decision-making information. This requires specific pieces of information needed to answer the marketing research problem. Managers must combine this information with their own experience and other information to make a proper decision. WD-40's marketing research problem was to gather information on how consumers clean and how they shop for cleaning products. The marketing research objective was several-fold: identify a better positioning strategy for X-14 and identify opportunities to add new items to the X-14 brand.

Whereas the marketing research problem is information oriented, the **management decision problem** is action oriented. Management problems tend to be much broader in scope and far more general than marketing research problems, which must be narrowly defined and specific if the research effort is to be successful. Sometimes several research studies must be conducted to solve a broad management problem. The management decision problem was: "How do we grow sales of X-14 family brand?" Management then decided to reposition X-14 as The Bathroom Expert—the

marketing research problem
Determining what information is needed and how that information can be obtained efficiently and effectively.

marketing research objective
The specific information needed to solve a marketing research problem; the objective should be to provide insightful decision-making information.

management decision problem
A broad-based problem that uses marketing research in order for managers to take proper actions.

centerpiece around which its new product line re-enters the market. Completely redesigned, the line establishes a family look for the set of products rather than a disjointed set of similar products. It also includes two additions: Foaming Bathroom Cleaner and Bathroom Cleaner, which combines oxy and citrus for general bathroom cleaning. Additionally, several new products will soon be released.[7]

SECONDARY DATA

secondary data
Data previously collected for any purpose other than the one at hand.

A valuable tool throughout the research process, but particularly in the problem/ opportunity identification stage is secondary data—data previously collected for any purpose other than the one at hand. Secondary information originating within the company includes documents such as annual reports, reports to stockholders, product testing results—perhaps made available to the news media—and house periodicals composed by the company's personnel for communication to employees, customers, or others. Often this information is part of a company's internal database.

Innumerable outside sources of secondary information also exist, principally coming from government departments and agencies (federal, state, and local) that compile and publish summaries of business data. Trade and industry associations also publish secondary data. Still more data are available in business periodicals and other news media that regularly publish studies and articles on the economy, specific industries, and even individual companies. The unpublished summarized secondary information from these sources corresponds to internal reports, memos, or special-purpose analyses with limited circulation. Economic considerations or priorities in the organization may preclude publication of these summaries. Most of the sources listed above can be found on the Internet.

Secondary data save time and money if they help solve the researcher's problem. Even if the problem is not solved, secondary data have other uses. They can aid in formulating the problem statement and suggest research methods and other types of data needed for solving the problem. In addition, secondary data can pinpoint the kinds of people to approach and their locations and serve as a basis of comparison for other data. The disadvantages of secondary data stem mainly from a mismatch between the researcher's unique problem and the purpose for which the secondary data were originally gathered, which are typically different. For example, a major consumer-products manufacturer wanted to determine the market potential for a fireplace log made of coal rather than compressed wood by-products. The researcher found plenty of secondary data about total wood consumed as fuel, quantities consumed in each state, and types of wood burned. Secondary data were also available about consumer attitudes and purchase patterns of wood by-product fireplace logs. The wealth of secondary data provided the researcher with many insights into the artificial log market. Yet, nowhere was there any information that would tell the firm whether consumers would buy artificial logs made of coal.

The quality of secondary data may also pose a problem. Often secondary data sources do not give detailed information that would enable a researcher to assess their quality or relevance. Whenever possible, a researcher needs to address these important questions: Who gathered the data? Why were the data obtained? What methodology was used? How were classifications (such as heavy users versus light users) developed and defined? When was the information gathered?

THE NEW AGE OF SECONDARY INFORMATION: THE INTERNET

Gathering secondary data, though necessary in almost any research project, has traditionally been a tedious and boring job. The researcher often had to write to government agencies, trade associations, or other secondary data providers and then wait days or weeks for a reply that might never come. Often, one or more trips to the library were required, and the researcher might find that needed reports were

Exhibit 9.3

Internet Search Topic Worksheet

Jot down a topic or subject you'd like to explore on the Web, and begin the presearch analysis:
1. **What UNIQUE WORDS, DISTINCTIVE NAMES, ABBREVIATIONS, or ACRONYMS are associated with your topic?** These may be the places to begin because their specificity will help you zero in on relevant pages.
2. **Can you think of societies, organizations, or groups that might have information on your subject via their pages?** Search these as a "phrase in quotes," looking for a home page that might contain links to other pages, journals, discussion groups, or databases on your subject. You may require the "phrase in quotes" to be in the document's title by preceding it by **title:[no space]**
3. **What other words are likely to be in ANY Web documents on your topic?** You may want to require these by joining them with **AND** or preceding each by **+[no space]**
4. **Do any of the words in 1, 2, or 3 belong in a phrase or string—together in a certain order, like a cliché?** Search these as a "phrase in quotes" (e.g., "observation research" or "marketing research aggregator").
5. **For any of the terms in 4, can you think of synonyms, variant spellings, or equivalent terms you would also accept in relevant documents?** You may want to allow these terms by joining them by **OR** and including each set of equivalent terms in **()** (e.g., surveys OR interviews).
6. **Can you think of any extraneous or irrelevant documents these words might pick up?** You may want to exclude terms or phrases with **– [no space]** before each term or use **AND NOT** (e.g., surveys or interviews –job).
7. **What BROADER terms could your topic be covered by?** When browsing subject categories or searching sites of webliographies or databases on your topic, try broader categories (e.g., marketing research).

SOURCE: Created by Joe Barker, Teaching Library, UC Berkeley.

checked out or missing. Now, however, the Internet has eliminated much of the drudgery associated with the collection of secondary data.

Finding Secondary Data on the Internet

Although there is probably no single best way to search the Web, we can recommend a five-step strategy:

- *Step One*: Analyze your topic to decide where to begin. A suggested worksheet is shown in Exhibit 9.3.
- *Step Two*: Test run a word or phrase in a search engine such as Google. Consider synonyms or equivalent terms.
- *Step Three*: Learn as you go and vary your approach with what you learn. Don't assume that you know what you want to find. Look at the search results and see what else you might use in addition to what you tried.
- *Step Four*: Don't get bogged down in a strategy that doesn't work. Consider using a subject directory. A few of the best are the Librarian's Index, **http://lii.org;** Infomine, **http://infomine.ucr.edu;** Academic Info, **http://www.academicinfo.net;** Google Directory, **http://directory.google.com;** About.com, **http://www.about.com;** and Yahoo Directory, **http://dir.yahoo.com.** Many researchers switch back and forth between directories and search engines.
- *Step Five:* For statistics and reports from more than 100 federal government agencies, go to: **http://www.fedstats.gov.** The agencies are listed alphabetically, and you can click on "key statistic" next to the agency's name to pull up links and other relevant information. Another good source for marketing researchers is **http:/www.secondarydata.com.** It organizes, indexes, and links the very best sources of free economic and marketing data. If you haven't found what you want, go back to the earlier steps better informed.[8]

Effective searching on the Internet is part art, part science, and part luck.

marketing research aggregator
A company that acquires, catalogs, reformats, segments, and resells reports already published by marketing research firms.

research design
Specifies which research questions must be answered, how and when the data will be gathered, and how the data will be analyzed.

primary data
Information that is collected for the first time; used for solving the particular problem under investigation.

Marketing Research Aggregators

The marketing research aggregator industry is a $120 million business that grows by roughly 6 percent a year. Companies in this field acquire, catalog, reformat, segment, and resell reports already published by large and small marketing research firms. Even Amazon.com has added a marketing research aggregation area to its high-profile e-commerce site.

The role of aggregator firms is growing because their databases of research reports are getting bigger and more comprehensive—and more useful—as marketing research firms get more comfortable using resellers as a sales channel. Meanwhile, advances in Web technology are making the databases easier to search and deliveries speedier. Research aggregators are also indirectly tapping new markets for traditional research firms. By slicing and repackaging research reports into narrower, more specialized sections for resale to small- and medium-sized clients that often cannot afford to commission their own studies or buy full reports, the aggregators are nurturing a new target market for the information.

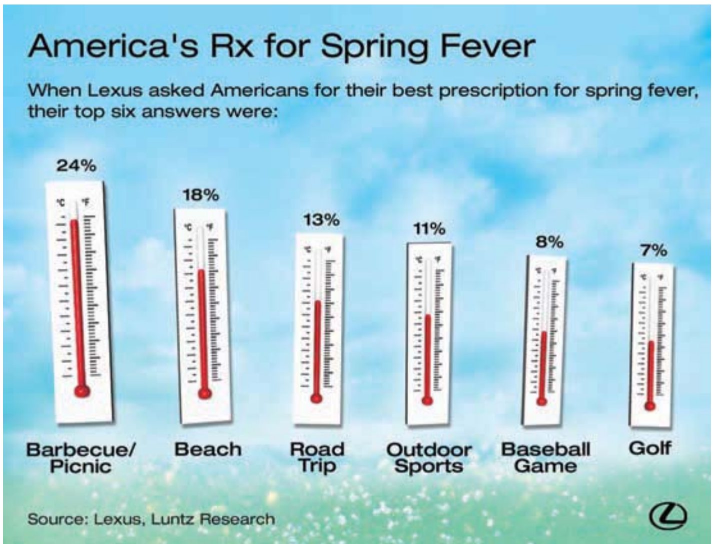
Prior to the emergence of research aggregators, a lot of marketing research was available only as premium-priced subscription services. For example, a 17-chapter $2,800 report from Wintergreen Research (based in Lexington, Massachusetts) was broken up and sold for $350 per chapter, significantly boosting the overall revenue generated by the report.

Other major aggregators are Marketingresearch.com, ProfoundBitpipe.com, and USADATA.com.

PLANNING THE RESEARCH DESIGN AND GATHERING PRIMARY DATA

Good secondary data can help researchers conduct a thorough situation analysis. With that information, researchers can list their unanswered questions and rank them. Researchers must then decide the exact information required to answer the questions. The research design specifies which research questions must be answered, how and when the data will be gathered, and how the data will be analyzed. Typically, the project budget is finalized after the research design has been approved.

Sometimes research questions can be answered by gathering more secondary data; otherwise, primary data may be needed. Primary data, or information collected for the first time, is used for solving the particular problem under investigation. The main advantage of primary data is that they will answer a specific research question that secondary data cannot answer. For example, suppose Pillsbury has two new recipes for refrigerated sugar cookie dough. Which one will consumers like better? Secondary data will not help answer this question. Instead, targeted consumers must try each recipe and evaluate the taste, texture, and appearance of each cookie. Moreover, primary data are current, and researchers know the source. Sometimes researchers gather the data themselves instead of assigning projects to outside companies. Researchers also specify the methodology of the research. Secrecy can be maintained for proprietary information. In contrast, much secondary data is available to all interested parties for relatively small fees or for free.



PRNEWSFOTO/© LEXUS

Companies gather primary data, like the survey results used in this Lexus advertisement, to collect new information directly from consumers. How do you think Lexus used the information it collected?

Gathering primary data is expensive; costs can range from a few thousand dollars for a limited survey to several million for a nationwide study. For instance, a nationwide, 15-minute telephone interview with 1,000 adult males can cost $50,000 for everything, including a data analysis and report. Because primary data gathering in person is so expensive, many firms now use an Internet study instead. Larger companies that conduct many research projects use another cost-saving technique. They *piggyback studies,* or gather data on two different projects using one questionnaire. The drawback is that answering questions about, say, dog food and gourmet coffee may be confusing to respondents. Piggybacking also requires a longer interview (sometimes a half hour or longer), which tires respondents. The quality of the answers typically declines, with people giving curt replies and thinking, "When will this end!" A lengthy interview also discourages people from participating in other research surveys.

Nevertheless, the disadvantages of primary data gathering are usually offset by the advantages. It is often the only way of solving a research problem. And with a variety of techniques available for research—including surveys, observations, and experiments—primary research can address almost any marketing question.

Survey Research

survey research
The most popular technique for gathering primary data, in which a researcher interacts with people to obtain facts, opinions, and attitudes.

mall intercept interview
A survey research method that involves interviewing people in the common areas of shopping malls.

The most popular technique for gathering primary data is survey research, in which a researcher interacts with people to obtain facts, opinions, and attitudes. Exhibit 9.4 summarizes the characteristics of traditional forms of survey research.

In-Home Personal Interviews

Although in-home personal interviews often provide high-quality information, they tend to be very expensive because of the interviewers' travel time and mileage costs. Therefore, they are rapidly disappearing from the American and European marketing researcher's survey toolbox. They are, however, still popular in many countries around the globe.

Mall Intercept Interviews

The mall intercept interview is conducted in the common area of a shopping mall or in a market research office within the mall. It is the economy version of the door-to-door interview; the interviewer has personal contact with the respondent, but saves on travel time and gas mileage. To conduct this type of interview, the research firm rents office space in the mall or pays a significant daily fee. One drawback is that it is hard to get a representative sample of the population this way.

However, an interviewer can also probe—or clarify a person's response—when necessary. For example, an interviewer might ask, "What did you like best about

Exhibit 9.4

Characteristics of Traditional Forms of Survey Research

Characteristic	In-Home Personal Interviews	Mall Intercept Interviews	Central Location Telephone Interviews	Self-Administered and One-Time Mail Surveys	Mail Panel Surveys	Executive Interviews	Focus Groups
Cost	High	Moderate	Moderate	Low	Moderate	High	Low
Time span	Moderate	Moderate	Fast	Slow	Relatively slow	Moderate	Fast
Use of interviewer	Yes	Yes	Yes	No	No	Yes	Yes
Ability to show concepts to respondent	Yes (also taste tests)	Yes (also taste tests)	No	Yes	Yes	Yes	Yes
Management control over interviewer	Low	Moderate	High	n/a	n/a	Moderate	High
General data quality	High	Moderate	High to moderate	Moderate to low	Moderate to low	High	Moderate
Ability to collect large amounts of data	High	Moderate	Moderate to low	Low to moderate	Moderate	Moderate	Moderate
Ability to handle complex questionnaires	High	Moderate	High, if computer-aided	Low	Low	High	N/A

the salad dressing you just tried?" The respondent might reply, "Taste." This answer doesn't provide a much information, so the interviewer could probe by saying, "Can you tell me a little bit more about taste?" The respondent might then elaborate: "Yes, it's not too sweet, it has the right amount of pepper, and I love that hint of garlic."

Mall intercept interviews must be brief. Only the shortest ones are conducted while respondents are standing. Usually, researchers invite respondents to their office for interviews, which generally take only 15 minutes. The researchers often show respondents concepts for new products or a test commercial or have them taste a new food product. The overall quality of mall intercept interviews is about the same as telephone interviews.

computer-assisted personal interviewing
An interviewing method in which the interviewer reads the questions from a computer screen and enters the respondent's data directly into the computer.

computer-assisted self-interviewing
An interviewing method in which a mall interviewer intercepts and directs willing respondents to nearby computers where the respondent reads questions off a computer screen and directly keys his or her answers into a computer.

central-location telephone (CLT) facility
A specially designed phone room used to conduct telephone interviewing.

Marketing researchers are applying computer technology in mall interviewing. The first technique is computer-assisted personal interviewing. The researcher conducts in-person interviews, reads questions to the respondent off a computer screen, and directly keys the respondent's answers into the computer. A second approach is computer-assisted self-interviewing. A mall interviewer intercepts and directs willing respondents to nearby computers. Each respondent reads questions off a computer screen and directly keys his or her answers into a computer.

Telephone Interviews Compared to the personal interview, the telephone interview costs less, but cost is rapidly increasing due to respondent refusals to participate. Most telephone interviewing is conducted from a specially designed phone room called a central-location telephone (CLT) facility. A phone room has many phone lines, individual interviewing stations, sometimes monitoring equipment, and headsets. The research firm typically will interview people nationwide from a single location. The federal "Do Not Call" law does not apply to survey research.

Most CLT facilities offer computer-assisted interviewing. The interviewer reads the questions from a computer screen and enters the respondent's data directly into the computer. The researcher can stop the survey at any point and immediately print out the survey results. Thus, a researcher can get a sense of the project as it unfolds and fine-tune the research design as necessary. An online interviewing system can also save time and money because data entry occurs as the response is recorded rather than as a separate process after the interview. Hallmark Cards found that an interviewer administered a printed questionnaire for its Shoebox Greeting cards in 28 minutes. The same questionnaire administered with computer assistance took only 18 minutes.

Mail Surveys Mail surveys have several benefits: relatively low cost, elimination of interviewers and field supervisors, centralized control, and actual or promised anonymity for respondents (which may draw more candid responses). Some researchers feel that mail questionnaires give the respondent a chance to reply more thoughtfully and to check records, talk to family members, and so forth. A disadvantage is that mail questionnaires usually have low response rates.

Low response rates pose a problem because certain elements of the population tend to respond more than others. The resulting sample may therefore not represent the surveyed population. For example, the sample may have too many retired people and too few working people. In this instance, answers to a question about attitudes toward government programs to aid senior citizens might indicate a much more favorable overall view of the system than is actually the case. Another serious problem with mail surveys is that no one probes respondents to clarify or elaborate on their answers.

Mail panels like those operated by Synovate, IPSOS, and NPD Research offer an alternative to the one-shot mail survey. A mail panel consists of a sample of households recruited to participate by mail for a given period. Panel members often receive gifts in return for their participation. Essentially, the panel is a sample used several times. In contrast to one-time mail surveys, the response rates from mail panels are high. Rates of 70 percent (of those who agree to participate) are not uncommon.

executive interviews
A type of survey that involves interviewing businesspeople at their offices concerning industrial products or services.

focus group
Seven to ten people who participate in a group discussion led by a moderator.

group dynamics
Group interaction essential to the success of focus-group research.

Executive Interviews Marketing researchers use executive interviews to conduct the industrial equivalent of door-to-door interviewing. This type of survey involves interviewing businesspeople, at their offices, concerning industrial products or services. For example, if Dell wanted information about user preferences for different features that might be offered in a new line of business computer printers, it would need to interview prospective user-purchasers of the printers. It is appropriate to locate and interview these people at their offices.

This type of interviewing is very expensive. First, individuals involved in the purchase decision for the product in question must be identified and located. Sometimes lists can be obtained from various sources, but more frequently screening must be conducted over the telephone. Even once a company likely to have the type of purchasers being sought is found, locating those people within a large organization can be expensive and time-consuming. Once a qualified person is located, the next step is to get that person to agree to be interviewed and to set a time for the interview. This is not as hard as it sounds because most professionals seem to enjoy discussing work-related topics.

Finally, an interviewer must go to the particular place at the appointed time. Long waits and cancellations are frequent occurances. This type of survey requires the very best interviewers because they are often interviewing on topics that they know very little about. Executive interviewing has essentially the same advantages and disadvantages as in-home interviewing.

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Focus groups can be used to gauge consumer response to a product or promotion and are occasionally used to brainstorm new product ideas.

Focus Groups A focus group is a type of personal interviewing. Often recruited by random telephone screening, typically seven to ten people with certain desired characteristics form a focus group. These qualified consumers are usually offered an incentive (typically \$50 to \$75) to participate in a group discussion. The meeting place (sometimes resembling a living room, sometimes featuring a conference table) has audiotaping and perhaps videotaping equipment. It also likely has a viewing room with a one-way mirror so that clients (manufacturers or retailers) can watch the session. A moderator, hired by the research company, leads the group discussion during the sesion.

Focus groups are much more than question-and-answer interviews. Market researchers draw a distinction between "group dynamics" and "group interviewing." The interaction provided by group dynamics is essential to the success of focus-group research; it is the reason for conducting group rather than individual research. One of the essential postulates of group-session usage is the idea that a response from one person may become a stimulus for another, thereby generating an interplay of responses that may yield more information than if the same number of people had contributed independently.

Lewis Stone, former manager of Colgate-Palmolive's Research and Development Division, says the following about focus groups:

> *If it weren't for focus groups, Colgate-Palmolive Co. might never know that some women squeeze their bottles of dishwashing soap, others squeeeeeze them, and still others squeeeeeeeeeeze out the desired amount. Then there are the ones who use the soap "neat." That is, they put the product directly on a sponge or washcloth and wash the dishes under running water until the suds run out. Then they apply more detergent.*

Stone explains how the body language, exhibited during focus groups, provides insights that would not show up in written responses to questions on habits and practices. Focus groups are a most efficient way to learn how one's products are actually used in the home. By drawing out the panelists to describe in detail how they perform certain tasks, you can learn a great deal about possible need-gaps that could be filled by new or improved products, and also how a new product might be received.[9]

A system created by Focus Vision Network allows client companies and advertising agencies to view live focus groups in over 350 cities worldwide. For example, the private satellite network lets a Taco Bell researcher observing a San Diego focus group control two cameras in the viewing room. The researcher can get a full-group view or a close-up, zoom, or pan the participants. The researcher can also communicate directly with the moderator using an ear receiver. Ogilvy & Mather (a large New York advertising agency whose clients include StarKist Sea Foods, Seagram's, MasterCard, and Burger King) use the system.

Increasingly, focus groups are being conducted online. Online focus groups are examined in detail later in the chapter.

Questionnaire Design

All forms of survey research require a questionnaire. Questionnaires ensure that all respondents will be asked the same series of questions. Questionnaires include three basic types of questions: open-ended, closed-ended, and scaled-response (see Exhibit 9.5). An **open-ended question** encourages an answer phrased in the respondent's own words. Researchers get a rich array of information based on the respondent's frame of reference. In contrast, a **closed-ended question** asks the respondent to make a selection from a limited list of responses. Traditionally, marketing researchers separate the two-choice question (called *dichotomous*) from the many-item type (often called *multiple choice*). A **scaled-response question** is a closed-ended question designed to measure the intensity of a respondent's answer.

open-ended question
An interview question that encourages an answer phrased in the respondent's own words.

closed-ended question
An interview question that asks the respondent to make a selection from a limited list of responses.

scaled-response question
A closed-ended question designed to measure the intensity of a respondent's answer.

Closed-ended and scaled-response questions are easier to tabulate than open-ended questions because response choices are fixed. On the other hand, unless the researcher designs the closed-ended question very carefully, an important choice may be omitted.

For example, suppose a food study asked this question: "Besides meat, which of the following items do you normally add to a taco that you prepare at home?"

Avocado	1	Olives (black/green)	6
Cheese (Monterey Jack/cheddar)	2	Onions (red/white)	7
Guacamole	3	Peppers (red/green)	8
Lettuce	4	Pimento	9
Mexican hot sauce	5	Sour cream	0

The list seems complete, doesn't it? However, consider the following responses: "I usually add a green, avocado-tasting hot sauce"; "I cut up a mixture of lettuce and spinach"; "I'm a vegetarian; I don't use meat at all. My taco is filled only with guacamole." How would you code these replies? As you can see, the question needs an "other" category.

Exhibit 9.5

Types of Questions Found on Questionnaires for National Market Research

Open-Ended Questions

1. What advantages, if any, do you think ordering from a mail-order catalog offers compared to shopping at a local retail outlet? (*Probe:* What else?)
2. Why do you have one or more of your rugs or carpets professionally cleaned rather than cleaning them yourself or having someone else in the household clean them?
3. What is it about the color of the eye shadow that makes you like it the best?

Closed-Ended Questions

Dichotomous

1. Did you heat the Danish product before serving it?
   Yes. 1
   No 2
2. The federal government doesn't care what people like me think.
   Agree. 1
   Disagree. 2

Multiple choice

1. I'd like you to think back to the last footwear of any kind that you bought. I'll read you a list of descriptions and would like for you to tell me which category they fall into. *(Read list and circle proper category.)*
   Dress and/or formal 1
   Casual 2
   Canvas/trainer/gym shoes 3
   Specialized athletic shoes 4
   Boots 5
2. In the last three months, have you used Noxzema skin cream . . . (Circle all that apply.)
   As a facial wash. 1
   For moisturizing the skin. 2
   For treating blemishes 3
   For cleansing the skin. 4
   For treating dry skin 5
   For softening skin. 6
   For sunburn 7
   For making the facial skin smooth 8

Scaled-Response Question

Now that you have used the rug cleaner, would you say that you . . . *(Circle one.)*

Would definitely buy it. 1
Would probably buy it 2
Might or might not buy it. 3
Probably would not buy it 4
Definitely would not buy it. 5

A good question should be clear and concise and avoid ambiguous language. Take, for example, the question "Do you live within ten minutes of here?" The answer depends on the mode of transportation (maybe the person walks), driving speed, perceived time, and other factors. Instead, respondents should see a map with certain areas highlighted and be asked whether they live in one of those areas.

Clarity also implies using reasonable terminology. A questionnaire is not a vocabulary test. Jargon should be avoided, and language should be geared to the target audience. A question such as "What is the level of efficacy of your preponderant dishwasher powder?" would probably be greeted by a lot of blank stares. It would be much simpler to say "Are you (1) very satisfied, (2) somewhat satisfied, or (3) not satisfied with your current brand of dishwasher powder?"

Stating the survey's purpose at the beginning of the interview also improves clarity. The respondents should understand the study's intentions and the interviewer's expectations. Sometimes, of course, to get an unbiased response, the interviewer must disguise the true purpose of the study. If an interviewer says, "We're conducting an image study for American National Bank" and then

© AP PHOTO/BOB CHILD

One interesting observation situation is toy-testing day camp. Pictured here, Fama Ana tries on a pair of "spy glasses" at Duracell Toy Testing Camp. In one week, over a thousand children in 15 cities tested 25 different toys while marketers watched.

proceeds to ask a series of questions about the bank, chances are the responses will be biased. Many respondents will try to provide answers that they believe are "correct" or that the interviewer wants to hear.

Finally, to ensure clarity, the interviewer should avoid asking two questions in one; for example, "How did you like the taste and texture of the Pepperidge Farm coffee cake?" This should be divided into two questions, one concerning taste and the other texture.

A question should also be unbiased. The question "Have you purchased any quality Black & Decker tools in the past six months?" biases respondents to think of the topic in a certain way (in this case, to link quality and Black & Decker tools). Questions can also be leading: "Weren't you pleased with the good service you received last night at the Holiday Inn?" (The respondent is all but instructed to say yes.) These examples are quite obvious; unfortunately, bias is usually more subtle. Even an interviewer's clothing or gestures can create bias.

Observation Research

In contrast to survey research, **observation research** depends on watching what people do. Specifically, it can be defined as the systematic process of recording the behavioral patterns of people, objects, and occurrences without questioning them. A market researcher using the observation technique witnesses and records information as events occur or compiles evidence from records of past events. Carried a step further, observation may involve watching people or phenomena and may be conducted by human observers or machines. Examples of these various observational situations are shown in Exhibit 9.6.

observation research
A research method that relies on four types of observation: people watching people, people watching an activity, machines watching people, and machines watching an activity.

mystery shoppers
Researchers posing as customers who gather observational data about a store.

Two common forms of people-watching-people research are one-way mirror observations and mystery shoppers.

At the Fisher-Price Play Laboratory, children are invited to spend 12 sessions playing with toys. Toy designers watch children to see how they react to Fisher-Price's and other makers' toys. A one-way mirror allows the researchers to see the participants and keeps the children from seeing the researchers. Fisher-Price, for example, had difficulty designing a toy lawn mower that children would play with. A designer, observing behind the mirror, noticed the children's fascination with soap bubbles. He then created a lawn mower that spewed soap bubbles. It sold over a million units in the first year.

Mystery shoppers are researchers posing as customers who gather observational data about a store (i.e., are the shelves neatly stocked?) and study customer/employee interactions. In the latter case, of course, there is communication between the mystery shopper and the employee. The mystery shopper may ask, "How much is this item?" "Do you have this in blue?" or "Can you deliver this by Friday?" The interaction is not an interview, and communication occurs only so that the

Exhibit 9.6

Observational Situations

Situation	Example
People watching people	Observers stationed in supermarkets watch consumers select frozen Mexican dinners; the purpose is to see how much comparison shopping people do at the point of purchase.
People watching phenomena	Observer stationed at an intersection counts traffic moving in various directions.
Machines watching people	Movie or videotape cameras record behavior as in the people-watching-people example above.
Machines watching phenomena	Traffic-counting machines monitor traffic flow.

mystery shopper can observe the actions and comments of the employee. Mystery shopping is, therefore, classified as an observational marketing research method even though communication is often involved.

Mystery shopping can provide a variety of benefits and insights, including:

- Enabling an organization to monitor compliance with product/service delivery standards and specifications (Eddie Bauer requires its sales staff to make three attempts to sell "add-ons" to each customer—would you like a tie, belt, and sunglasses to go with that shirt).
- Enabling marketers to examine the gap between promises made through advertising/sales promotion and actual service delivery.
- Helping monitor the impact of training and performance improvement initiatives.
- Identifying differences in the customer experience across different times of day, locations, product/service types and other potential sources of variation in product/service quality.[10]

At a posh Coach showroom in midtown Manhattan, Sylvia Morse is leaving no accessory unturned. Pursuing the perfect gift for her mother—or so she claims—she scrutinizes everything from a $300 handbag to a tiny fabric photo locket. A sales associate helps her figure out which colors match the store's signature hot magenta leather goods.

But beneath her bubbly exterior, Morse isn't satisfied. "The first greeting took a good long time," she mutters. As she stands near the shoe shelf, ostensibly ogling a pair of low-top leather sneakers, she spots at least two groups of loitering saleswomen, too intent on one another's gossip to pay her any attention. Her leisurely stroll around the floor attracts little notice, and when she finally decides to purchase the handbag for "Mom," the cashier is brusque. "Fourteen sales associates in there and only one gave me the time of day," she says to herself, "and *she* barely followed up." Soon she'll fill out a detailed online survey form that will report her experience at the Manhattan store to Coach management. Sylvia is a mystery shopper![11]

Ethnographic Research

ethnographic research
The study of human behavior in its natural context; involves observation of behavior and physical setting.

Ethnographic research comes to marketing from the field of anthropology. The technique is becoming increasingly popular in commercial marketing research. Ethnographic research, or the study of human behavior in its natural context, involves observation of behavior and physical setting. Ethnographers directly observe the population they are studying. As "participant observers," ethnographers use their intimacy with the people they study to gain richer, deeper insights into culture and behavior—they try to understand what makes people do what they do. Ethnographers often question those they observe to gain a fuller understanding of what they are seeing.

Ethnographers can record:

- what happens, including what objects are created or manipulated
- where it is happens
- flow of what is happening
- order of what is happens
- the length of events
- who does what
- verbal and nonverbal communications
- reactions of the various participants (which are critical)[12]

Volkswagen recently used ethnography to investigate the U.S. car market. Among the insights gathered are that Americans like lots of storage space in their vehicles, and as many stereo speakers as possible. While Germans prize a car's driving capability and frown on eating while driving, ethnographers found that Americans think of their cars as a second home or office, frequently using fast food drive-throughs and eating in their cars. This finding led the researchers to recommend adding cup holders to new VWs.[13]

Kimberly-Clark, makers of Huggies, Kleenex, and other household staples, has taken a slightly different twist in its ethnographic research. Ethnographers have outfitted consumers with mini video cameras mounted to visors and linked to a recording device. Paid participants wear the gear, known internally as the Consumer Vision System (CVS), while doing chores or shopping.

Using the system, K-C discovered that mothers who used Huggies Baby Wash, a bathing lotion, had trouble holding the bottle and needed two hands to open and dispense its contents. "[Moms] almost always have to have one hand on the baby at one time," said Becky Walter, K-C director-innovation, design and testing.[14] K-C redesigned the product with a grippable bottle and a large lid that could easily be lifted with a thumb. Walters declined to disclose figures, but said that repackaging helped the brand rebound in market share.[15]

Experiments

experiment
A method a researcher uses that alters one or more variables while observing the effect on another variable (typically sales).

An **experiment** is a method a researcher can use to gather primary data. The researcher alters one or more variables—price, package design, shelf space, advertising theme, advertising expenditures—while observing the effects of those alterations on another variable (usually sales). The best experiments are those in which all factors are held constant except the ones being manipulated. The researcher can then observe that changes in sales, for example, result from changes in advertising spending.

GLOBAL Perspectives

Ethnographic Insights from South of the Border

Martha Rivera, an ethnographer for Doyle Research Associates in Chicago, conducts studies in Latin America. A few of her insights are:

During a study conducted in Venezuela, in an ordinary bathroom I saw a large multicolored, perfectly round sphere made of small bits of body soap. The interviewee explained that he usually compressed together these bits of body soap when they had become too small. All subsequent participants were asked what they regularly did with the last pieces of their body soap. Most of them automatically placed the old small piece to the new soap bar without another thought. Supplementary questions revealed that the flat form of the client's soap bar was thought to facilitate this, and that these consumers actually looked for that particular brand for that reason. Hence the client abandoned its plan to change the shape of its soap.

While testing a new type of package for pre-prepared meat, Mexican housewives claimed that they would readily buy any pre-prepared food item because it offered the convenience that they reportedly expected from all types of products. However, it was observed that their refrigerators were filled exclusively with fresh food items, thus suggesting that these housewives habitually prepared their meals from scratch and did not consume any form of pre-prepared food.

While visiting Colombian housewives to learn about their habits related to the preparation of empanadas (which are fried, filled pastries, similar to burritos but fully enclosed and small) I noticed that most of them stored cooking oil right next to a solid version of the same product which is considerably cheaper and performs the same function but lessens the flavor of the food. (Both varieties are regularly consumed in low-income households, but housewives tend to save the liquid oil for special plates.) Many reported frying the empanada with liquid oil; however, as they began taking out the ingredients from their pantries, some interviewees glanced at the solid oil and decided to use it instead of the liquid. When asked about this change in their habits, they related that seeing the solid oil was a reminder of the higher price of the liquid and led them to prefer the solid.[16]

Could this type of information have just as easily been gathered by focus groups? Internet surveys? How?

From Martha Rivera, "An Enriching Process", 'Quirk's Marketing Research Review', November 2005, 30-37.

Holding all other factors constant in the external environment is a monumental and costly, if not impossible, task. Factors like competitors' actions, weather, and economic conditions are beyond the researcher's control. Yet market researchers have ways to account for the ever-changing external environment. Mars, the candy company, was losing sales to other candy companies. Traditional surveys showed that the shrinking candy bar was not perceived as a good value. Mars wondered whether a bigger bar sold at the same price would increase sales enough to offset the higher ingredient costs. The company designed an experiment which kept the marketing mix the same in different markets but varied the size of the candy bar. The substantial increase in sales of the bigger bar quickly proved that the additional costs would be more than covered by the additional revenue. Mars increased the bar size—and its market share and profits.

SPECIFYING THE SAMPLING PROCEDURES

Once the researchers decide how they will collect primary data, their next step is to select the sampling procedures they will use. A firm can seldom take a census of all possible users of a new product, nor can it interview all of them. Therefore, a firm must select a sample of the group to be interviewed. A sample is a subset from a larger population.

Several questions must be answered before a sampling plan is chosen. First, the population, or universe, of interest must be defined. This is the group from which the sample will be drawn. It should include all the people whose opinions, behavior, preferences, attitudes, and so on are of interest to the marketer. For example, in a study whose purpose is to determine the market for a new canned dog food, the universe might be defined as all current buyers of canned dog food.

After the universe has been defined, the next question is whether the sample must be representative of the population. If the answer is yes, a probability sample is needed. Otherwise, a nonprobability sample might be considered.

sample
A subset from a larger population.

universe
The population from which a sample will be drawn.

probability sample
A sample in which every element in the population has a known statistical likelihood of being selected.

random sample
A sample arranged in such a way that every element of the population has an equal chance of being selected as part of the sample.

nonprobability sample
Any sample in which little or no attempt is made to get a representative cross section of the population.

convenience sample
A form of nonprobability sample using respondents who are convenient or readily accessible to the researcher—for example, employees, friends, or relatives.

measurement error
An error that occurs when there is a difference between the information desired by the researcher and the information provided by the measurement process.

Probability Samples

A probability sample is a sample in which every element in the population has a known statistical likelihood of being selected. Its most desirable feature is that scientific rules can be used to ensure that the sample represents the population.

One type of probability sample is a random sample—a sample arranged in such a way that every element of the population has an equal chance of being selected as part of the sample. For example, suppose a university is interested in getting a cross section of student opinions on a proposed sports complex to be built using student activity fees. If the university can acquire an up-to-date list of all the enrolled students, it can draw a random sample by using random numbers from a table (found in most statistics books) to select students from the list. Common forms of probability and nonprobability samples are shown in Exhibit 9.7.

Nonprobability Samples

Any sample in which little or no attempt is made to get a representative cross-section of the population can be considered a nonprobability sample. Therefore the probability of selection of each sampling unit is not known. A common form of a nonprobability sample is the convenience sample, which uses respondents who are convenient or readily accessible to the researcher—for instance, employees, friends, or relatives.

Nonprobability samples are acceptable as long as the researcher understands their nonrepresentative nature. Because of their lower cost, nonprobability samples are the basis of much marketing research.

Types of Errors

Whenever a sample is used in marketing research, two major types of errors may occur: measurement error and sampling error. Measurement error occurs when

Exhibit 9.7

Types of Samples

	Probability Samples
Simple Random Sample	Every member of the population has a known and equal chance of selection.
Stratified Sample	The population is divided into mutually exclusive groups (such as gender or age); then random samples are drawn from each group.
Cluster Sample	The population is divided into mutually exclusive groups (such as geographic areas); then a random sample of clusters is selected. The researcher then collects data from all the elements in the selected clusters or from a probability sample of elements within each selected cluster.
Systematic Sample	A list of the population is obtained—i.e., all persons with a checking account at XYZ Bank—and a *skip interval* is obtained by dividing the sample size by the population size. If the sample size is 100 and the bank has 1,000 customers, then the skip interval is 10. The beginning number is randomly chosen within the skip interval. If the beginning number is 8, then the skip pattern would be 8,18, 28, ...
	Nonprobability Samples
Convenience Sample	The researcher selects the easiest population members from which to obtain information.
Judgment Sample	The researcher's selection criteria are based on personal judgment that the elements (persons) chosen will likely give accurate information.
Quota Sample	The researcher finds a prescribed number of people in several categories—i.e., owners of large dogs versus owners of small dogs. Respondents are not selected on probability sampling criteria.
Snowball Sample	Additional respondents are selected on the basis of referrals from the initial respondents. This method is used when a desired type of respondent is hard to find—i.e., persons who have taken round-the-world cruises in the last three years. This technique employs the old adage "Birds of a feather flock together."

there is a difference between the information desired by the researcher and the information provided by the measurement process. For example, people may tell an interviewer that they purchase Coors beer when they do not. Measurement error generally tends to be larger than sampling error.

sampling error
An error that occurs when a sample somehow does not represent the target population.

frame error
An error that occurs when a sample drawn from a population differs from the target population.

random error
An error that occurs when the selected sample is an imperfect representation of the overall population.

Sampling error occurs when a sample somehow does not represent the target population. Sampling error can be one of several types. Nonresponse error occurs when the sample actually interviewed differs from the sample drawn. This error happens because the original people selected to be interviewed either refused to cooperate or were inaccessible. For example, people who feel embarrassed about their drinking habits may refuse to talk about them.

Frame error, another type of sampling error, arises if the sample drawn from a population differs from the target population. For instance, suppose a telephone survey is conducted to learn Chicago beer drinkers' attitudes toward Coors. If a Chicago telephone directory is used as the *frame* (the device or list from which the respondents are selected), the survey will contain a frame error. Not all Chicago beer drinkers have a phone, and many phone numbers are unlisted. An ideal sample (for example, a sample with no frame error) matches all important characteristics of the target population to be surveyed. Could you find a perfect frame for Chicago beer drinkers?

Random error occurs when the selected sample is an imperfect representation of the overall population. Random error represents how accurately the chosen sample's true average (mean) value reflects the population's true average (mean) value. For example, we might take a random sample of beer drinkers in Chicago and find that 16 percent regularly drink Coors beer. The next day we might repeat the same sampling procedure and discover that 14 percent regularly drink Coors beer. The difference is due to random error.

Error is common to all surveys, yet it is often not reported or is underreported. Typically, the only error mentioned in a written report is sampling error. When errors are ignored, misleading results can lead to poor information and, perhaps, bad decisions.

COLLECTING THE DATA

field service firm
A firm that specializes in interviewing respondents on a subcontracted basis.

cross-tabulation
A method of analyzing data that lets the analyst look at the responses to one question in relation to the responses to one or more other questions.

Marketing research field service firms collect most primary data. A field service firm specializes in interviewing respondents on a subcontracted basis. Many have offices, often in malls, throughout the country. A typical marketing research study involves data collection in several cities, requiring the marketer to work with a comparable number of field service firms. Besides conducting interviews, field service firms provide focus-group facilities, mall intercept locations, test product storage, and kitchen facilities to prepare test food products.

ANALYZING THE DATA

After collecting the data, the marketing researcher proceeds to the next step in the research process: data analysis. The purpose of this analysis is to interpret and draw conclusions from the mass of collected data. The marketing researcher tries to organize and analyze those data by using one or more techniques common to marketing research: one-way frequency counts, cross-tabulations, and more sophisticated statistical analysis. Of these three techniques, one-way frequency counts are the simplest. One-way frequency tables record the responses to a question. For example, the answers to the question "What brand of microwave popcorn do you buy most often?" would provide a one-way frequency distribution. One-way frequency tables are always done in data analysis, at least as a first step, because they provide the researcher with a general picture of the study's results.

A cross-tabulation, or "cross-tab," lets the analyst look at the responses to one question in relation to the responses to one or more other questions. For example, what is the association between gender and the brand of microwave popcorn bought most frequently? Hypothetical answers to this question are shown in Exhibit 9.8.

Although the Orville Reddenbacher brand was popular with both males and females, it was more popular with females. Compared with women, men strongly preferred Pop Rite, whereas women were more likely to buy Weight Watchers popcorn.

Researchers can use many other more powerful and sophisticated statistical techniques, such as hypothesis testing, measures of association, and regression analysis. A description of these techniques goes beyond the scope of this book, but can be found in any good marketing research textbook. The use of sophisticated statistical techniques depends on the researchers' objectives and the nature of the data gathered.

PREPARING AND PRESENTING THE REPORT

After data analysis has been completed, the researcher must prepare the report and communicate the conclusions and recommendations to management. This is a key step in the process. If the marketing researcher wants managers to carry out the recommendations, he or she must convince them that the results are credible and justified by the data collected.

Researchers are usually required to present both written and oral reports on the project. Today, the written report is no more than a copy of the PowerPoint slides used in the oral presentation. Both reports should be tailored to the audience. They should begin with a clear, concise statement of the research objectives, followed by a complete, but brief and simple, explanation of the research design or methodology employed. A summary of major findings should come next. The conclusion of the report should also present recommendations to management.

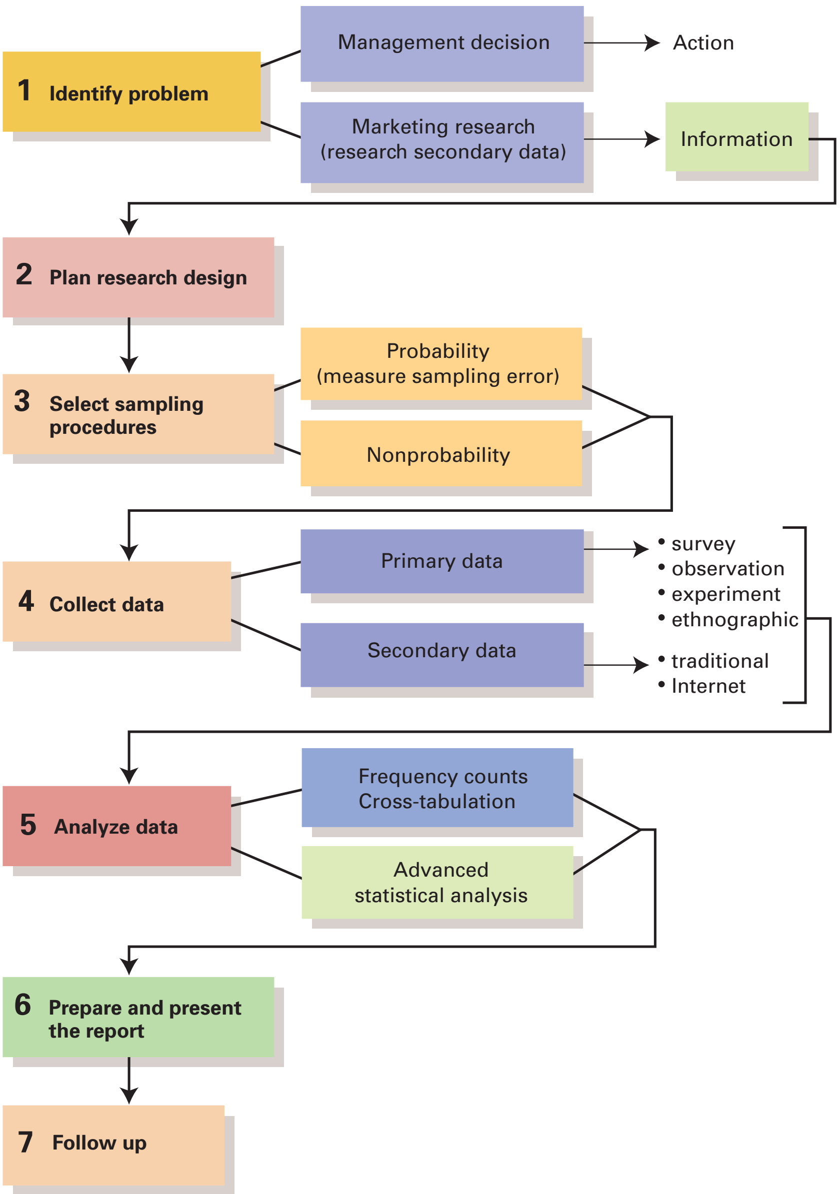
Exhibit 9.8

Hypothetical Cross-Tabulation between Gender and Brand of Microwave Popcorn Purchased Most Frequently

	Purchase by Gender	
Brand	Male	Female
Orville Reddenbacher	31%	48%
T.V. Time	12	6
Pop Rite	38	4
Act Two	7	23
Weight Watchers	4	18
Other	8	0

REVIEW LEARNING OUTCOME

LO3 Describe the steps involved in conducting a marketing research project



Most people who enter marketing will become research users rather than research suppliers. Thus, they must know what to notice in a report. As with many other items we purchase, quality is not always readily apparent. Nor does a high price guarantee superior quality. The basis for measuring the quality of a marketing research report is the research proposal. Did the report meet the objectives established in the proposal? Was the methodology outlined in the proposal followed? Are the conclusions based on logical deductions from the data analysis? Do the recommendations seem prudent, given the conclusions?

FOLLOWING UP

The final step in the marketing research process is to follow up. The researcher should determine why management did or did not carry out the recommendations in the report. Was sufficient decision-making information included? What could have been done to make the report more useful to management? A good rapport between the product manager, or whoever authorized the project, and the market researcher is essential. Often they must work together on many studies throughout the year.

LO4 The Profound Impact of the Internet on Marketing Research

The Internet has forever changed the way survey research is conducted. The vast majority (88 percent) of U.S. research firms are now conducting marketing research online.[17]

In the United States, the online population now closely tracks the United States population in most key demographic areas. In 2007, over 175 million Americans logged on each month to shop, e-mail, find information, visit in chat rooms, and so forth.[18] As Internet penetration rises, the demographic profile of Internet users continues to look more like that of the nation as a whole. It is still true that more young than older people, and more affluent than low-income people, are online. However, 8 percent of Internet users are now age 65 or over (compared to 16 percent of all adults ages 65 or over), 39 percent of Internet users did not go to college (compared to 47 percent of all adults), and 14 percent have incomes below $25,000 (compared to 19 percent of all adults).[19] As the number of Internet users continues to grow worldwide (currently about 1.2 billion), the characteristics of a country's population and its Internet users tend to meld.[20]

There are several reasons for the success of Internet marketing research:

- It facilitates better and faster decision making by speeding up access to business intelligence.
- It improves the ability to respond quickly to customer needs and market shifts.
- It makes follow-up studies and tracking research much easier to conduct and more fruitful.
- It slashes labor- and time-intensive research activities (and associated costs), including mailing, telephone solicitation, data entry, data tabulation, and reporting.

ADVANTAGES OF INTERNET SURVEYS

The huge growth in the popularity of Internet surveys is the result of the many advantages offered by the Internet. The specific advantages of Internet surveys are related to many factors:

- *Rapid development, real-time reporting*: Internet surveys can be broadcast to thousands of potential respondents simultaneously. Respondents complete surveys immediately; then results are tabulated and posted for corporate clients to view as the returns arrive. The result: survey results can be in a client's hands in significantly less time than would be required for traditional surveys.
- *Dramatically reduced costs*: The Internet can cut costs by 25 to 40 percent and provide results in half the time it takes to do traditional telephone surveys. Data collection costs account for a large proportion of any traditional market research budget. Telephone surveys are labor-intensive efforts incurring training, telecommunications, and management costs. Electronic methods eliminate these completely. While costs for traditional survey techniques rise proportionally with the number of interviews desired, electronic solicitations can grow in volume with little increase in project costs.
- *Personalized questions and data*: Internet surveys can be highly personalized for greater relevance to each respondent's own situation, thus speeding the response process. Respondents enjoy a personalized survey because they are asked to answer only pertinent questions, can pause and resume the survey as needed, and can see previous responses and correct inconsistencies.
- *Improved respondent participation*: Busy respondents may be growing increasingly intolerant of "snail mail" or telephone-based surveys. Internet surveys take half as much time to complete as phone interviews, can be accomplished at the respondent's convenience (after work hours), and are much more stimulating and engaging. Graphics, interactivity, links to incentive sites and real-time summary reports make the interview enjoyable. The result? Much higher response rates.
- *Contact with the hard-to-reach*: Certain groups—doctors, high-income professionals, top management in Global 2000 firms—are among the most surveyed on the planet and the most difficult to reach. Many of these groups are well represented online. Internet surveys provide convenient anytime/anywhere access, making it easy for busy professionals to participate.

USES OF THE INTERNET BY MARKETING RESEARCHERS

Marketing researchers use the Internet to administer surveys, conduct focus groups and observation research, and perform a variety of other types of marketing research.

Common Types of Internet Samples

Internet samples can be classified as screened or recruited.

screened Internet sample An Internet sample with quotas based on desired sample characteristics.

recruited Internet sample A sample in which respondents are prerecruited and must qualify to participate. They are then e-mailed a questionnaire or directed to a secure Web site.

Screened Internet samples Screened Internet samples adjust for the unrepresentativeness of the self-selected respondents by imposing quotas based on some desired sample characteristics. These are often demographic characteristics such as gender, income, and geographic region, or product-related criteria such as past purchase behavior, job responsibilities, or current product use.

Screened sample questionnaires typically use a branching or skip pattern for asking screening questions to determine whether the full questionnaire should be presented to a respondent. Some Web survey systems can make immediate market segment calculations that first assign a respondent to a particular segment based on screening questions and then select the appropriate questionnaire to match the respondent's segment.

Recruited Internet Samples Recruited Internet samples are used in surveys that require more control over the makeup of the sample. Recruited samples are ideal for applications in which there is already a database from which to recruit the sample. For example, a good application would be a survey that used a customer database to recruit respondents for a purchaser satisfaction study.

Respondents are recruited by telephone, mail, or e-mail, or in person. After qualification, they are sent the questionnaire by e-mail or are directed to a Web site with a link to the questionnaire. At Web sites, passwords are normally used to restrict access to the questionnaire to recruited sample members. Since the makeup of the sample is known, completions can be monitored; to improve the participation rate, follow-up messages can be sent to those who have not completed the questionnaire.

Recruited Panels By far, the most popular form of Internet sampling is the recruited panel. In the early days of Internet recruiting, panels were created by means of Web-based advertising that offered compensation for participation in online studies. This method allowed research firms to build large pools of individuals who were available to respond quickly to the demands of online marketing research. Internet panels have grown rapidly and now account for over 50 percent of all custom research sampling in the United States.

Renting Internet Panels Very few marketing research companies build their own Internet panels because of the huge expense involved. Instead, they rent a sample from an established panel provider. The largest and oldest sample provider in the nation is Survey Sampling, Inc. Today, it offers the marketing research industry a huge Internet panel called Survey Spot with over 5 million members. As with its other (non-Internet) panels, Survey Sampling offers subsets of its main panel, which is balanced demographically. In other words, its panel looks exactly like the U.S. population in terms of demographics, based on the U.S. Census. Some of the subsets of the main panel are shown in Exhibit 9.9.

Exhibit 9.9

Survey Spot Allows Precise Targeting

1. Geography
2. Income
3. Race
4. Shopping Preferences
5. Occupation
6. Education
7. Gender
8. "Intenders" (i.e., intend to buy a car)
9. Age
10. Ailments & Medical Conditions
11. Hobbies
12. Automotive Characteristics
13. Investors
14. Personal Travel
15. Interests
16. Business Travel
17. Electronics
18. Lifestyles
19. Sports

SOURCE: Survey Sampling, Inc.

Online Focus Groups

A recent development in qualitative research is the online focus group. A number of organizations are currently offering this new means of conducting focus groups. The process is fairly simple.

- The research firm builds a database of respondents via a screening questionnaire on its Web site.
- When a client comes to a firm with a need for a particular focus group, the firm goes to its database and identifies individuals who qualify. It sends an e-mail message to these individuals, asking them to log on to a particular site at a particular time scheduled for the group. The firm pays them an incentive for their participation.
- The firm develops a discussion guide similar to the one used for a conventional focus group.
- A moderator runs the group by posting questions online for all to see. The group operates in an environment similar to that of a chat room so that all participants see all questions and all responses.
- The firm captures the complete text of the focus group and makes it available for review after the group has finished.

The Moderator's Role The basic way the moderator communicates with respondents in an online focus group is "freestyle" or "on the fly." That is, the moderator types in all questions, instructions, and probes into the text-entry area of the chat room in real-time (live, on-the-spot). In a variation on this method, the moderator copies and pastes questions from an electronic version of the guide into the text-entry area. Here, the moderator will toggle back and forth between the document and the chat room. An advantage of the freestyle method is that it forces the moderator to adapt to the group instead of using a series of canned questions. A disadvantage is that typing everything freestyle (or even copying and pasting from a separate document) takes time.

One way respondents can see stimuli (e.g., a concept statement, a mockup of a print ad, or a short product demonstration video) is for the moderator to give the respondents a URL. Respondents then copy the URL from the chat stream, open another browser window, paste in the URL, and view it. An advantage of this approach is its simplicity. However, there are several disadvantages. First, if the respondents do not copy the URL correctly, they will not see it. Another disadvantage is that once respondents open another browser, they have "left the room" and the moderator has lost their attention; researchers must hope that respondents will return within the specified amount of time.

More advanced virtual focus group software reserves a frame (section) of the screen for stimuli to be shown. Here, the moderator has control over what is shown in the stimulus area. The advantage of this approach is that the respondent does not have to do any work to see the stimuli.

Types of Online Focus Groups Decision Analyst, one of America's most progressive firms in applying Internet technology to marketing research, offers two types of online focus groups:

1. *Real-time online focus groups*: These are live, interactive sessions with four to six participants and a moderator in a chat room format. The typical session does not last longer than 45 to 50 minutes. This technique is best for simple, straightforward issues that can be covered in limited time. The results tend to be superficial compared to in-person focus groups—but this is acceptable for certain types of projects. Typically, three to four groups are recommended as a minimum. Clients can view the chat room as the session unfolds and communicate with the moderator.

2. *Time-extended online focus groups*: These sessions follow a message board format and usually last five to ten days. The 15 to 20 participants must comment at least two or three times per day and spend 15 minutes a day logged in to the discussion. The moderator reviews respondents' comments several times per day (and night) and probes or redirects the discussion as needed. This technique provides three to four times as much content as the average in-person focus group. Time-extended online focus groups give participants time to reflect, talk to others, visit a store, or check the pantry. This extra time translates into richer content and deeper insights. Clients can view the online content as it is posted and may communicate with the moderator at any time.[21]

Using Channel M2 to Conduct Online Focus Groups Channel M2 provides market researchers with user-friendly virtual interview rooms, recruiting, and technical support for conducting virtual qualitative research, efficiently and effectively. By using Channel M2, the moderator and client can see and hear every respondent. You can see a demo at **http://www.channelM2.com.**

To recruit focus groups (from a global panel with access to over 15 million online consumers), Channel M2 uses a blend of e-mail and telephone verification and confirmation. Specifically, e-mails elicit involvement and direct participants to an online qualification questionnaire to ensure that each meets screening criteria. Telephone follow-up confirms that respondents qualify. Participants are sent a Web camera so that both verbal and nonverbal reactions can be recorded. Channel M2 tech support helps participants install the Webcam one to two days prior to the interview. Before participating, respondents must show a photo ID (their driver's license) to their Webcam to verify their identity.

Participants are then provided instructions via e-mail, including a link to the Channel M2 interviewing room and a toll-free teleconference number to call. Upon clicking the link, participants sign on and see the Channel M2 interview room, complete with live video of the other participants, text chat, screen or slide sharing, and whiteboard (see Exhibit 9.10).

Thus, in a Channel M2 focus group, all the participants can see and hear each other and communicate in a group setting. Once the focus group is under way, questions and answers occur in "real time" in a lively setting. Participants comment spontaneously, both verbally and via text messaging, yet the moderator can provide direction exactly as would be done in a traditional setting.[22]

Advantages of Online Focus Groups Many advantages are claimed for cyber groups. Cyber Dialogue, a marketing research company specializing in cyber groups, lists the following benefits of online focus groups on its Web site:

- *Speed*: Typically, focus groups can be recruited and conducted, with delivery of results, within five days of client approval.
- *Cost-effectiveness*: Off-line focus groups incur costs for facility rental, airfare, hotel, and food. None of these costs is incurred with online focus groups.
- *Broad geographic scope*: In a given focus group, you can speak to people in Boise, Idaho, and Miami, Florida, at the same time.
- *Accessibility*: Online focus groups give you access to individuals who otherwise might be difficult to recruit (e.g., business travelers, doctors, mothers with infants).
- *Honesty*: From behind their screen names, respondents are anonymous to other respondents and tend to talk more freely about issues that might create inhibitions in a face-to-face group.

Exhibit 9.10

An M2 Online Focus Group Under Way

SOURCE: From http://www.ChannelM2.com accessed November, 2005

The Role of Consumer Generated Media in Marketing Research

Consumer generated media
Media which is consumer generated and shared with other consumers

Consumer generated media (CGM) is that media which consumers generate themselves and share among themselves. Because it is consumer-based, it is trusted more than traditional forms of advertising and promotion.[23] CGM originates from:

- Blogs
- Message boards and forums
- Public discussions (Usenet newsgroups)
- Discussions and forums on large email portals (Yahoo!, AOL, MSN)
- Online opinion/review sites and services
- Online feedback/complaint sites
- Shared videos and photos
- Podcasts

It is estimated that 2 billion CGM comments are archived on the Web today. That number grows by about 30 percent annually.[24]

CGM can be influenced but not controlled by marketers. To influence CGM, one must first understand what is being said or shown. Nielsen BuzzMetrics is the leading marketing research firm tracking CGM. The firm uses sophisticated data mining and other technologies to help marketers understand what is being said about their company and brands on the Web. BrandPulse is BuzzMetrics' most popular product. BrandPulse can tell a company about the spread and influence of CGM. How much "buzz" exists? Where is online discussion taking place, and by whom? What issues are most important? Is the tone of discussion negative or positive?

BrandPulse enables clients to listen in on unaided consumer conversations that take place on Internet forums, boards, Usenet newsgroups and blogs, providing timely understanding of the opinions and trends affecting a company or brand.

A second product, BrandPulse Insight, focuses on specific issues and concerns such as:

- What's the buzz about a certain issue, trend, product, or piece of news?
- Who's active online, and what are these online consumers saying?
- Are current trends building or waning?
- Can any emerging trends be detected early, before they catch fire (or fizzle out prematurely)?
- What key motivators influence and affect consumer behavior?
- What are consumer/customer moods and emotions regarding a particular topic or a specific brand?
- Which online consumers are likely candidates for influencer panels and relationship marketing programs?[25]

A marketer wanting to know about the latest diet trends, technological gadgets, automotive perceptions, or health-related concerns can tap into BrandPulse Insights to understand what's being said.

Nielsen BuzzMetrics offers a free service entitled BlogPulse, **http://www.blogpulse.com,** which is a blog search engine and a trend tracker. You can easily create your own graphs plotting blog buzz by entering a search term. Alternatively, you can check out popular blog trends, follow a story trail between two bloggers, or see profiles of popular bloggers.

behavioral targeting
A form of observation marketing research that uses data mining coupled with identifying Web surfers by their IP addresses plus demographic/psychographic profiles.

Behavioral Targeting Using Marketing Research

Behavioral targeting is a form of observation marketing research that uses data mining coupled with identifying Web surfers by their IP addresses. It then obtains data such as gender, age, and geographic area from databases provided by firms like Tacoda, Revenue Science, and Quantcast to predict which text ad, banner ad, or marketing email is most likely to make the Web surfer click. Thus, behavioral targeting combines records of a consumer's online activities with psychographic/demographic profiles.

Companies using behavioral targeting include Allstate, American Express, IBM, and TDAmeritrade. When Pepsi wanted to make a splash on the Web to promote its new low-calorie vitamin-enhanced water, Aquafina Alive, the company didn't run ads just anywhere on the Internet. It used behavioral targeting and placed ads only on sites it knew would be visited by people interested in healthy lifestyles.

Pepsi worked with Tacoda to identify health-conscious people by looking at traffic to sites about healthy lifestyles over a month-long period. Then Pepsi arranged to place Aquafina Alive ads on some of the 4,000 Web sites affiliated with Tacoda so the ads would pop up whenever these health-conscious consumers visited. The result? Pepsi recorded a three-fold increase in the number of people clicking on its Aquafina Alive ads compared with previous campaigns.[26] Pepsi's success explains why behavioral targeting advertising was over $1 billion in 2008.[27]

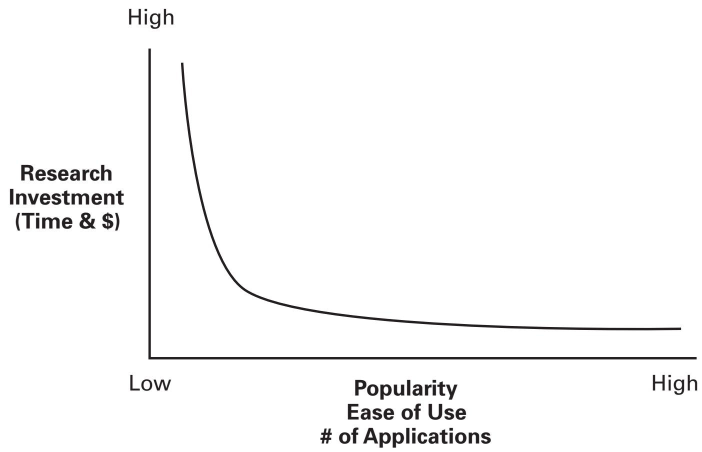
Other Uses of the Internet by Marketing Researchers

The Internet revolution in marketing research has influenced more than just the way surveys and focus groups are conducted. It also enhanced the management of the research process and the dissemination of information. Several key areas have been affected by the Internet:

- *The distribution of requests for proposals (RFPs) and proposals*: Companies can now quickly and efficiently send RFPs to a select e-mail list of research suppliers. In turn, research suppliers can develop proposals and e-mail them back to clients. A process that used to take days using snail mail now occurs in a matter of hours.
- *Collaboration between the client and the research supplier in the management of a research project*: Now a researcher and client can both look at a proposal, RFP, report, or statistical analysis on their respective computer screens while they discuss it over the telephone. This is very powerful and efficient. Changes in the sample size, quotas, and other aspects of the research plan can be discussed and made immediately.
- *Data management and online analysis*: Clients can access their survey via the research supplier's secure Web site and monitor the data gathering in real time. The client can use sophisticated tools to perform data analysis as the survey develops. This real-time analysis may result in changes in the questionnaire, sample size, or the types of respondents being interviewed. The research supplier and the client become partners in "just-in-time" marketing research.

REVIEW LEARNING OUTCOME

LO4 Discuss the profound impact of the Internet on marketing research



By driving down time and cost of collecting data, the Internet has increased in popularity, has become easier to use, and therefore is used in a growing number of research applications.

scanner-based research
A system for gathering information from a single group of respondents by continuously monitoring the advertising, promotion, and pricing they are exposed to and the things they buy.

BehaviorScan
A scanner-based research program that tracks the purchases of 3,000 households through store scanners in each research market.

- *Publication and distribution of reports*: Reports can be published to the Web directly from programs such as PowerPoint and all the latest versions of leading word-processing, spreadsheet, and presentation software packages. This means that results are available to appropriate managers worldwide on an almost instantaneous basis. Reports can be searched for the content of interest using the same Web browser used to view the report.
- *Viewing of oral presentations of marketing research surveys by widely scattered audiences*: By placing oral presentations on password-protected Web sites, managers throughout the world can see and hear the actual client presentation. This saves time and money by avoiding the need for the managers to travel to a central meeting site.[28]

LO5

Scanner-Based Research

Scanner-based research is a system for gathering information from a single group of respondents by continuously monitoring the advertising, promotion, and pricing they are exposed to and the things they buy. The variables measured are advertising campaigns, coupons, displays, and product prices. The result is a huge database of marketing efforts and consumer behavior. Scanner-based research approaches the Holy Grail of marketing research: an accurate, objective picture of the direct causal relationship between different kinds of marketing efforts and actual sales.

© PHOTODISC/GETTY IMAGES

IRI's BehaviorScan product allows IRI to track individual household purchases over time. Participants in the household panel present an ID card at the checkout of a scanner-equipped grocery store.

The two major scanner-based suppliers are Information Resources, Inc. (IRI), and the A. C. Nielsen Company. Each has about half the market. However, IRI is the founder of scanner-based research.

IRI's first product is called BehaviorScan. A household panel (a group of 3,000 long-term participants in the research project) has been recruited and maintained in each BehaviorScan town. Panel members shop with an ID card, which is presented at the checkout in scanner-equipped grocery stores and drugstores, allowing IRI to electronically track each household's purchases, item by item, over time. It uses microcomputers to measure TV viewing in each panel household and can send special commercials to panel members' television sets. With such a measure of household purchasing, it is possible to manipulate marketing variables, like TV advertising or consumer promotions, or to introduce a new product and analyze real changes in consumer buying behavior.

IRI's most successful product is InfoScan—a scanner-based sales-tracking service for the consumer packaged-goods industry. Retail sales, detailed consumer purchasing information (including measurement of store loyalty and total grocery basket expenditures), and promotional activity by manufacturers and retailers are monitored and evaluated for all bar-coded products. Data are collected weekly from more than 34,000 supermarkets, drugstores, and mass merchandisers.

When Should Marketing Research Be Conducted?

InfoScan
A scanner-based sales-tracking service for the consumer packaged-goods industry.

When managers have several possible solutions to a problem, they should not instinctively call for marketing research. In fact, the first decision to make is whether to conduct marketing research at all.

Some companies have been conducting research in certain markets for many years. Such firms understand the characteristics of target customers and their likes and dislikes about existing products. Under these circumstances, further research would be repetitive and wasteful. Procter & Gamble, for example, has extensive knowledge of the coffee market. After it conducted initial taste tests with Folgers Instant Coffee, P&G went into national distribution without further research. Consolidated Foods Kitchen of Sara Lee followed the same strategy with its frozen croissants, as did Quaker Oats with Chewy Granola Bars. This tactic, however, does not always work. P&G marketers thought they understood the pain reliever market thoroughly, so they bypassed market research for Encaprin aspirin in capsules. Because it lacked a distinct competitive advantage over existing products, however, the product failed and was withdrawn from the market.

Managers rarely trust their judgment enough to refuse more information so long as it is available and free. But they might have enough confidence that they would be unwilling to pay very much for the information or to wait a long time to receive it. The willingness to acquire additional decision-making information depends on managers' perceptions of its quality, price, and timing. Of course, if perfect information were available—that is, the data conclusively showed which alternative to choose—decision makers would be willing to pay more for it than for information that still left uncertainty. In summary, research should be undertaken only when the expected value of the information is greater than the cost of obtaining it.

REVIEW LEARNING OUTCOME

LO5 Discuss the growing importance of scanner-based research

BehaviorScan	InfoScan
Panel information from specific groups of people, enables researchers to manipulate variables and see real results	Aggregate consumer information on all bar-coded products

LO6 Competitive Intelligence

Derived from military intelligence, competitive intelligence is an important tool for helping a firm overcome a competitor's advantage. Specifically, competitive intelligence helps identify the advantage and determine how it was achieved.

competitive intelligence (CI) An intelligence system that helps managers assess their competition and vendors in order to become more efficient and effective competitors.

Competitive intelligence (CI) helps managers assess their competitors and their vendors in order to become a more efficient and effective competitor. Intelligence is analyzed information. It becomes decision-making intelligence when it has implications for the organization. For example, one of your firm's primary competitors may have plans to introduce a product with performance standards equal to your own but with a 15 percent cost advantage. The new product will reach the market in eight months. This intelligence has important decision-making and policy consequences for management. Competitive intelligence and environmental scanning (gathering data about the external environment—see Chapter 4) combine to create marketing intelligence. Marketing intelligence is then used as input in a marketing decision support system. Nine out of ten large companies have employees dedicated to the CI function. Many firms spend several million dollars a year on it.

The top corporate CI officer at a multibillion-dollar global technology company claims that competitive intelligence helped his company recover after it began losing market share to a competitor. The rival, after competing directly with the company for years, had figured out its bidding strategy. Instead of competing on price with an off-the-shelf offering, the rival offered prospects a customized solution—and it was winning. When the CI officer's company changed to a customized approach, it won hundreds of millions of dollars in new business. CI helped win Pergo, Inc., a maker of laminate flooring, a major contract. When Pergo told a national retailer what it had learned from a mutual supplier—that the rival would not be able to launch a new product when it said it would—the retailer signed with Pergo instead.

Conferences and professional courses led by rival executives are great places to gather information. A former competitive intelligence chief at telecom-software vendor Telcordia, says his firm hit the jackpot when one of its accountants attended a professional course taught by a competitor's CFO. The CFO used his company as the case for the class, revealing all kinds of tantalizing private financial information. Listening in on competitors' presentations to analysts at investment conferences and on conference calls is another good way to get financial data.

Executives, marketers and engineers tend to enjoy talking about what's new or emerging at their companies. Talking to these people at trade shows or even watching regulatory proceedings can yield fruitful CI. When drugmaker Bristol-Myers Squibb (BMS) told Congress it needed to increase its harvest of environmentally sensitive yew trees, says a former intelligence executive at SmithKline Beecham, he knew there was a good chance that BMS would soon seek Food and Drug Administration approval for a drug using yew bark.

SOURCES OF COMPETITIVE INTELLIGENCE

The Internet and its databases are a great source of CI. CI researchers can use Internet databases to answer these and other questions:

- What articles were written about this market?
- What companies are associated with this product group?
- What patents have been filed for this technology?
- What are the major magazines or texts in this industry?
- What are the chances that I will find something in print on the target company?
- How many companies are in the same industry as the target company?
- Who are the reporters studying this industry?
- How can I be updated on industry and company events without having to constantly request the information?
- How can I compile a list of the leading experts in the industry and the key institutions they are associated with?

Non-computer-based sources of CI can be found in a variety of areas:

- A company's salespeople, who can directly observe and ask questions about the competition.
- Experts with in-depth knowledge of a subject or activity.
- CI consultants, who can use their knowledge and experience to gather needed information quickly and efficiently.
- Government agencies, a valuable source of all types of data.
- Uniform Commercial Code (UCC) filings, a system that identifies goods that are leased or pledged as collateral. This is an excellent source for learning about a company's latest additions to plant assets.
- Suppliers, a group that may offer information on products shipped to a competitor.

REVIEW LEARNING OUTCOME

LO 6 Explain the concept of competitive intelligence

CI

- Part of a sound marketing strategy
- Helps companies respond to competitive threats
- Helps reduce unnecessary costs

- Periodicals, a good source for timely articles on successes, failures, opportunities, and threats.
- The Yellow Pages, which often provide data on a number of competitors, trading areas, and special offerings.
- Trade shows, official gatherings where competitors display their latest offerings.

This list is not exhaustive, but it does provide an idea of how CI can be gathered.

$7 billion < amount that U.S. marketers spend on research each year

ounces of ketchup consumed by children each year > **5 billion**

$2,800 < cost of a 17-chapter report from Wintergreen Research aggregators

cost of a single chapter > **$350**

$50,000 < cost of a 15-minute telephone interview with 1,000 men

minutes required to complete a printed questionnaire for Hallmark's Shoebox Greeting Cards > **28**

18 < minutes required to complete the same questionnaire with computer assistance

88 < percentage of U.S. research firms conducting marketing research online

members on the Internet panel Survey Spot > **5 million**

34,000 < stores from which InfoScan tracks data

Review and Applications

LO 1

Explain the concept and purpose of a marketing decision support system. A decision support system (DSS) makes data instantly available to marketing managers and allows them to manipulate the data themselves to make marketing decisions. Four characteristics make DSSs especially useful to marketing managers: (1) They are interactive, flexible, discovery oriented, and accessible; (2) They give managers access to information immediately and without outside assistance; (3) They allow users to manipulate data in a variety of ways and to answer "what if" questions; (4) They are user-friendly even for computer novices.

1.1 In the absence of company problems, is there any reason to develop a marketing DSS?

1.2 Explain the difference between marketing research and a DSS.

LO 2

Define marketing research and explain its importance to marketing decision making. Marketing research is the process of collecting and analyzing data in order to solve specific marketing problems. Marketers use marketing research to explore the profitability of marketing strategies. They can examine why particular strategies failed and analyze characteristics of specific market segments. Managers can use research findings to retain current customers. Moreover, marketing research allows management to behave proactively, rather than reactively, by identifying newly emerging patterns in society and the economy.

2.1 The task of marketing is to create exchanges. What role might marketing research play in the facilitation of the exchange process?

2.2 Marketing research has traditionally been associated with manufacturers of consumer goods. Today, however, an increasing number of organizations, both profit and nonprofit, use marketing research. Why? Give some examples of specific reasons for organizations to use marketing research.

WRITING

2.3 Write a reply to the following statement: "I own a restaurant in the downtown area. Every day, I see customers whom I know on a first-name basis. I understand their likes and dislikes. If I put something on the menu and it doesn't sell, I know that they didn't like it. I also read the magazine *Modern Restaurants* to follow industry trends. This is all of the marketing research I need to do."

2.4 Give an example of (a) the descriptive role of marketing research, (b) the diagnostic role, and (c) the predictive function of marketing research.

LO3 **Describe the steps involved in conducting a marketing research project.** The marketing research process involves several basic steps. First, the researcher and the decision maker must agree on a problem statement or set of research objectives. The researcher then creates an overall research design specifying how primary data will be gathered and analyzed. Before collecting data, the researcher decides whether the group to be interviewed will be a probability or nonprobability sample. Field service firms are often hired to carry out data collection. Once data have been collected, the researcher analyzes them using statistical analysis. The researcher then prepares and presents oral and written reports, with conclusions and recommendations, to management. As a final step, the researcher determines whether the recommendations were implemented and what could have been done to make the project more successful.

3.1 Critique the following methodologies and suggest more appropriate alternatives:

- **a.** A supermarket was interested in determining its image. It dropped a short questionnaire into the grocery bag of each customer before putting in the groceries.
- **b.** To assess the extent of its trade area, a shopping mall stationed interviewers in the parking lot every Monday and Friday evening. Interviewers walked up to people after they had parked their cars and asked them for their ZIP codes.
- **c.** To assess the popularity of a new movie, a major studio invited people to call a 900 number and vote yes, they would see it again, or no, they would not. Each caller was billed a $2 charge.

WRITING

3.2 You have been charged with determining how to attract more business majors to your school. Write an outline of the steps you should take, including the sampling procedures, to accomplish the task.

3.3 Why are secondary data sometimes preferable to primary data?

3.4 What is a marketing research aggregator? What role do these aggregators play in marketing research?

3.5 Discuss when focus groups should and should not be used.

TEAM

3.6 Divide the class into teams of eight persons. Each team will conduct a focus group on the quality and number of services that your college provides for its students. One person from each team should be chosen to act as moderator. Remember, it is the moderator's job to facilitate discussion, not lead it. These group sessions should last approximately 45 minutes. If possible, the groups should be videotaped or recorded. Upon completion, each team should write a brief report of its results. Consider offering to meet with the dean of students to share the results of your research.

3.7 Why do companies hire mystery shoppers?

3.8 Ethnographic research is a new (and expensive) trend in marketing research. Find an article on ethnographic research. Read and summarize it. What is your opinion of ethnographic research? Do you think it will be the wave of the future? Explain your reasoning.

LO4 **Discuss the profound impact of the Internet on marketing research.** The Internet has vastly simplified the secondary data search process, placing more sources of information in front of researchers than ever before. Internet survey research is surging in popularity. Internet surveys can be created rapidly and reported in real time. They are also relatively inexpensive and easily personalized. Often researchers can use the Internet to contact respondents who are difficult to reach by other means. The Internet can also be used to conduct focus groups, analyze consumer-generated media, engage in behavioral targeting, distribute research proposals and reports, and to facilitate collaboration between the client and the research supplier. Clients can access real-time data and analyze the information as the collection process continues.

ONLINE

4.1 Go to **http://www.SRIC-bi.com** and take the VALS Survey. Report on how marketing researchers use this information.

TEAM

4.2 Divide the class into teams. Each team should go to a different opt-in survey site on the Web and participate in an online survey. A spokesperson for each team should report the results to the class.

4.3 What are various ways to obtain respondents for online surveys?

4.4 Describe the advantages and disadvantages of online surveys.

LO5 **Discuss the growing importance of scanner-based research.** A scanner-based research system enables marketers to monitor a market panel's exposure and reaction to such variables as advertising, coupons, store displays, packaging, and price. By analyzing these variables in relation to the panel's subsequent buying behavior, marketers gain useful insight into sales and marketing strategies.

5.1 Why has scanner-based research been seen as "the ultimate answer" for marketing researchers? Do you see any disadvantages of this methodology?

5.2 Detractors claim that scanner-based research is like "driving a car down the road looking only in the rearview mirror." What does this mean? Do you agree?

LO6 **Explain the concept of competitive intelligence.** Competitive intelligence (CI) helps managers assess their competition and their vendors in order to become more efficient and effective competitors. Intelligence is analyzed information, and it becomes decision-making intelligence when it has implications for the organization.

By helping managers assess their competition and vendors, CI leads to fewer surprises. CI allows managers to predict changes in business relationships, guard against threats, forecast a competitor's strategy, and develop a successful marketing plan.

The Internet and databases accessed via the Internet offer excellent sources of CI. Company personnel, particularly sales and service representatives, are usually good sources of CI. Many companies require their salespersons to routinely fill out CI reports. Other external sources of CI include experts, CI consultants, government agencies, UCC filings, suppliers, newspapers and other publications, the Yellow Pages, and trade shows.

6.1 Why do you think that CI is so hot in today's environment?

WRITING

6.2 Prepare a memo to your boss at JetBlue Airlines to outline why the organization needs a CI unit.

TEAM

6.3 Form teams of three students. Each team must choose a firm in the PC manufacturing industry and then go to the firm's Web site and acquire as much CI as possible. Each team will then prepare a five-minute oral presentation on its findings.

Key Terms

Exercises

APPLICATION EXERCISE

For its study, *Teens and Healthy Eating: Oxymoron or Trend?*, New York–based BuzzBack Market Research focused on snacking. Among its findings: Teens eat an average of three snacks per day; breakfast is the meal they skip most often. Though scads of snacks are stacked on store shelves, when it comes to healthier treats targeting adolescents, it's a bit of a teenage wasteland. BuzzBack asked 532 teen respondents to imagine new foods they'd gobble up. The following are some of their ideas:

- "Travel fruit. Why can't fruit be in travel bags like chips or cookies? Canned fruit is too messy. Maybe have a dip or something sold with it, too."—Female, age 17.
- "A drink that contains five servings of fruits and vegetables."—Male, age 16, Caucasian.
- "I would invent all natural and fat-free, vitamin-enhanced cookies and chips that had great flavor."—Female, age 16.
- "I would make fruit-based cookies."—Male, age 16, Caucasian.
- "Low-carb trail mix, because trail mix is easy to eat but it has a lot of fat/carbs."—Female, age 15, Caucasian.
- "I would create some sort of microwavable spaghetti."—Male, age 16, Caucasian.
- "Something quick and easy to make that's also cheap. I'll be in college next year, and I'm trying to find things that are affordable, healthier than cafeteria food, and easy to make."—Female, age 17.
- "*Good* vegan mac n'cheese."—Female, age 18, Caucasian.
- "A smoothie where you could get all the nutrients you need, that tastes good, helps you stay in shape, and is good for you. Has vitamins A, B_3, B_{12}, C, ginkgo. Packaging would be bright."—Female, age 16, African American.
- "A breakfast shake for teens. Something easy that tastes good, not necessarily for dieters like Slim Fast, etc. Something to balance you off in the morning."—Male, age 18.[29]

Activities

1. You are a new-product development specialist at Kraft. What guidance can you get from the BuzzBack study?
2. Choose one of the suggestions from the above list of healthy snack concepts. Imagine that your company is interested in turning the idea into a new product but wants to conduct market research before investing in product development. Design a marketing research plan that will give company managers the information they need before engaging in new-product development of the idea. (Hint: Use steps 1–3 in Exhibit 9.2 as a guide.)
3. Once you have finished your plan, collect the data. Depending on the data-collection methods you have outlined in your plan, you may need to make adjustments so that you can collect actual data to analyze.
4. Analyze the data you collected and create a report for your company either recommending that the company pursue the idea you chose or investigate another.

ETHICS

ETHICS EXERCISE

John Michael Smythe owns a small marketing research firm in Cleveland, Ohio, which employs 75 people. Most employees are the sole breadwinners in their families. John's firm has not fared well for the past two years and is on the verge of bankruptcy. The company recently surveyed over 2,500 people in Ohio about new-car purchase plans for the Ohio Department of Economic Development. Because the study identified many hot prospects for new cars, a car dealer has offered John \$8,000 for the names and phone numbers of people saying they are "likely" or "very likely" to buy a new car within the next 12 months. John needs the money to avoid laying off a number of employees.

Questions

1. Should John Smythe sell the names?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketingpower.com** and review the ethics statement. Then write a brief paragraph on what the AMA Statement of Ethics contains that relates to John Smythe's dilemma.

Case Study: Red Lobster

MARKET RESEARCH REVEALS WHAT'S FRESH TODAY

Remember the Red Lobster commercials featuring lots of fried shrimp bouncing around and lobster claws dripping with butter? They've been replaced by scenes of steaming fresh fish, rice and vegetables. The old slogan, "For the Seafood Lover in You" has also been canned. Now Red Lobster wants you to "Come See What's Fresh Today." The restaurants themselves will soon look different, too, with a streamlined, contemporary décor that downplays their traditional nautical themes.

These changes and more are part of an effort to makeover the seafood chain after marketing research revealed that the restaurant was considered outdated and unappealing to potential customers. Red Lobster president Kim Ludrop says that in the first stage of the makeover, the chain improved operations so that customers wouldn't have to wait so long for the food to reach their table. The second phase focused on improving the restaurant's image and shifting the focus from low prices to freshness. The third and final challenge will be to increase sales. Lodrup says, "We are positioning Red Lobster to be the best seafood restaurant on the planet."

Lodrup was originally hired as a marketing specialist to revive the sagging brand's image in 2003 when sales were falling and customer satisfaction was at an all-time low. He immediately put the kibosh on promotions like the All-You-Can-Eat Crab Legs Specials that had lost money for the company in the past and emphasized Red Lobster's seafood expertise instead. After sales increased in 2004, he was promoted to president, but he still relies on marketing research to keep his finger on the pulse of customer preferences.

"We find out what they want from idealized dining service and research how to deliver value to guests," Lodrup says. To do that, Red Lobster follows changing consumer habits and notes which dishes patrons prefer. They use phone and Internet surveys to learn about guest attitudes towards the food they've tried and try to determine how well they might respond to new menu items or concept changes before instituting them. The guest-relations department "catalogs the nature of guest contact so we can see if there are changes in trends," Lodrup explains. "Emerging concerns or requests from consumers get captured weekly and recorded for our executives."

More in-depth research measures attitudes and trends that could affect the brand in the future. Before a promotion is launched, featured menu items are chosen through extensive consumer testing. Beginning with a large number of possible dishes, they narrow it down to the one that testers deem most appealing.

After studies indicated that freshness is the single biggest criteria consumers use to judge a seafood restaurant, the chain knew it was vital to get word out that fresh fish is delivered to Red Lobster restaurants six days a week. Interviews with former customers revealed that many still believed that Red Lobster's fish was frozen despite the company's extensive global connections and rapid seafood delivery system.

"It's really important to signal to people food is freshly prepared," says marketing V.P. Salli Setta, who created the Culinary Institute of Tuscany for Olive Garden before Red Lobster hired him. The company is considering a similar seafood-related school in Maine to add authenticity to Red Lobster's menu. In the meantime, Setta hired a new team of executive chefs to create updated recipes with the herbs that customers said had fresher connotations than the traditional lemon and butter sauces.

They also introduced a separate Fresh Fish Menu that is updated twice a day at the restaurants. Even though fresh fin fish had been on the regular menu for years, it had never really been promoted. Research showed that this could make the restaurant more appealing to their lapsed customers, who tend to be affluent, educated, and over 50. Households with an annual income of more than $70,000 account for half of all food eaten in restaurants and have demonstrated interest in seafood dining. Reeling these customers back in has become a top priority in the chain's turnaround.

So far the makeover is working. Red Lobster has been reporting same-store sales increases since 2004. Improvements in operations and other cost controls led to the highest operating margin in Red Lobster history and, Lodrup reports, "Every measure of guest satisfaction is at a record level." However, it continues to be a challenge for the chain to change old perceptions of itself. As one surveyed customer put it, "My wife swears by the fish. She just can't get her friends to try it." [30]

Questions

1. Why do you think Red Lobster relies so much on Internet surveys to track customer opinions, preferences, and criticisms? What are the advantages of online questionnaires versus traditional surveys conducted over the phone or through the mail?
2. Go to **www.redlobster.com** and click around. How well do you think the site appeals to the educated, affluent, and over-50 crowd that the chain wants to reel in? What are the primary messages that it communicates about the restaurant, and how effective are they? How does the site attempt to capture information about its customers?
3. Red Lobster's closest competitor in the seafood-dining business is Joe's Crab Shack. Check out their Web site at **www.joescrabshack.com** and compare it to Red Lobster's. How does their marketing approach differ? Do you think they're appealing to the same types of customers? How does the Web site try to get information from its customers?
4. Suppose Red Lobster wondered how well its new interior design was received by customers at a redecorated restaurant in Columbus, Ohio, and hired you to create a questionnaire. Write one of each: an open-ended question, a closed-ended question (either dichotomous or multiple choice), and a scaled-response question.

Company Clips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READYMADE—READY RESEARCH

Having been in business for five years, ReadyMade now has a lot of research on the various characteristics of its readers. Its knowledge of GenNesters has made the magazine a leader in identifying and describing that segment. As a new business, ReadyMade found that businesses had little interest in marketing to this group. Now that businesses have become more aware of GenNester influence, however, ReadyMade is able to fill the need for information. ReadyMade has statistics on the ages at which people are marrying and the interests of recently-married couples that have just married. Because the magazine is ahead of the curve on gathering information on this segment, ReadyMade can help other businesses figure out how to tailor their marketing efforts to fit the needs of GenNesters.

Questions

1. How has ReadyMade been able to help Toyota promote its new line of cars? What benefit has ReadyMade seen from the partnership?
2. How does ReadyMade use new technology to gain information about its consumers?
3. What sorts of long-term decisions is ReadyMade making that could be aided by research? What would you recommend?

Marketing & You Results

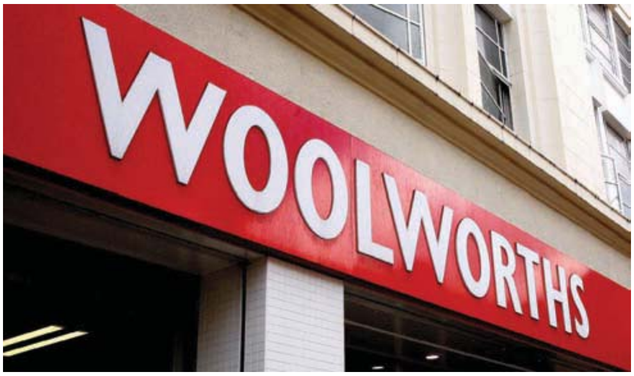
Higher scores indicate that you place greater importance on collecting primary and secondary information when developing marketing campaigns or projects. A lower score means you would be less aggressive in collecting information and might plow ahead regardless of how much information you do (or don't) have. After reading Chapter 9, you can see how involved gathering and analyzing market information can be, but also how critical it is to success.

Marketing Miscue

What's in the Lolita Name?

In 1955, Vladimir Nabokov wrote a book called *Lolita*. The novel became famous worldwide for its controversial topic; the narrator and protagonist is sexually obsessed with a 12-year-old girl. In addition to becoming one of the most controversial classics of twentieth-century literature, the book was adapted to film in both 1962 and 1997. Over time, the name "Lolita" has entered into pop culture as a phrase for a sexually precocious young girl.

More than a half-century later, Woolworths, a chain of retail stores in the United Kingdom, began offering the Lolita Midsleeper Combi on its retail Web site. This bedroom set, comprised of a whitewashed wooden bed with pull-out desk and a cupboard, was targeted to young girls at a retail price of £395. Woolworths, operating as an online retailer, allows direct sellers to offer products on the Woolworths Web site. The direct seller then delivers the product directly to consumers. Thus, Woolworths is not in possession of many products on its Web site, and these products are not listed as Woolworths brands.



©AP PHOTO

On January 30, 2008, Catherine Hanly, editor of **Raisingkids.co.uk,** an online parents' forum, saw the Lolita furniture on the Woolworths retail site. She immediately alerted parents via the Raisingkids online forums by asking, "Am I being particularly sensitive, or does anyone else out there think it's bad taste for Woolies to have a kiddy bed range named 'Lolita'?" Additionally, Hanly contacted the press department at Woolworths asking them to comment on the product's name.

Within a few hours of being contacted by Hanly, Woolworths removed the product offering from its retail Web site. According to a Woolworths' spokesperson, the staff running the Web site was unfamiliar with the classic novel and the connotations behind the name itself. As reported by **Raisingkids.co.uk**, a Woolworths' press officer was quoted as saying, "This was one product sold online and in the Big Red Book and quite naturally the people who arranged it had no idea about that word. They'd never heard of the word and in fact, neither had I. I had to go to Wikipedia to find out the meaning of that word."

Evidently, the Web site forum had considerable influence on the removal of the product from the Woolworths Web site. Additionally, the forum exchanges allowed parents (consumers) to debate the issue surrounding a product name. Naturally, many of the blogs centered on the fact that a name synonymous with sexual precocity was tied to a young girl's bed. Other bloggers commented on the denial of Woolworths regarding the name's connotation. Some bloggers reported that both DVD versions of the Lolita film (Stanley Krubrick's classic 1962 version and the 1997 remake starring Jeremy Irons) were available for purchase on the Woolworths retail site; they had trouble believing that the name and subsequent retail site posting were inadvertent mistakes. Other bloggers, however, questioned the idea of attaching a meaning to a girl's name. One blogger noted that Lolita is a very common Hispanic name, citing that of a childhood friend named Lolita-Marie. Another blogger added that Lolita is the name of a style trend in Japan. Apparently, this particular Japanese sub-culture promotes an elegant Gothic Lolita style of prettiness and elegance, but not sexuality. Still others questioned whether personal names should be banned from public use once they are associated with negativity.

Discussions surrounding the naming of the Lolita bedroom furniture also brought forth other retail concerns about branding. In 2005, retailer WH Smiths had sold stationery targeted to youth with a Playboy bunny. In 2003, British Home Stores (BHS) was criticized for selling its Little Miss Naughty padded bras and underwear to pre-teen girls. The Bratz dolls are criticized for being flagrantly sexualized, as well as for encouraging children to be bratty.

Questions:

1. Where does the name of a product enter into the consumer decision making process?
2. Should a company conduct marketing research prior to naming a product?

Critical Thinking Case

The Course at Eagle Mountain

(http://www.thecourseateaglemountain.com) is a championship golf course located on the banks of the beautiful White River in the foothills of the Ozark Mountains in Batesville, Arkansas. Batesville is listed in "The 100 Best Small Towns in America" by *Norman Crampton*, a nationwide guide to the best in small living in America. The owners hope to market the golf course and Batesville as a destination for tourism, as well as a major player in the retirement community marketplace.

Tourism

Destination marketing demands that the purveyor understands the target market, answering questions such as "What satisfies visitors?" and "What keeps them coming back?" Naturally, the owners are especially interested in the vacationer who wants to combine golf with an overall outdoor vacation experience. Often referred to as "The Natural State," Arkansas offers 15 golf courses on the Natural State Golf Trail.

Highlighting its motto, of "The most beautiful drives are in Arkansas," the goal is to make Arkansas the natural choice for golf vacations. Bill Siegel, chairman of Longwoods International, expounds on the potential for success of regional destinations. In a 2004 *Travel Weekly* article, Siegel states, "People take a lot of trips during a year, most of them short and most of them regional. Some of the highest return-on-investment numbers come from places that don't necessarily have a sterling reputation on a wish list. A lot more people go to New Jersey beaches than to Hawaii beaches."

© PHOTODISC/GETTY IMAGES

However, The Natural State is not alone in its efforts to create tourism around golfing. There are over 850 golf courses in an egg-shaped area from Chicago, Illinois to Baton Rouge, Louisiana and Nashville, Tennessee to Oklahoma City, Oklahoma. An overview of promotional material suggests that golfers look for three main characteristics when deciding which course to visit: playability (some golfers just cannot play the same courses that professionals play, while others relish the opportunity to play those courses); price (there appears to be a price-quality relationship); and prestige (ranging from private to semi-private to public).

Retirement Communities

The baby boom generation is in the throes of the retirement process. As a market segment, there are about 77 million boomers and almost one-half of them are over 50 years of age. These 50- to 60-year-old boomers spend more than $2 trillion annually. The disposable income of this age segment has prompted a need for luxury vacation/retirement homes.

Reaching this demographic has never been easier. Surfing the Internet for homes is common among this "silver surfing" market segment. These retiring boomers are sophisticated, affluent, and active. They want retirement communities with clubhouses, billiard rooms, cafes, walking trails, gyms, outdoor activities, and an active social community. Two interesting baby boom trends in retirement living have emerged. First, boomers tend to retire close to where their adult lives were spent. Second, many choose pack retirement (purchasing retirement homes in the same community as their friends).

The Golf Demographic

According to the National Golf Foundation, the average household income of a golfer is almost $20,000 higher than the average U.S. household income. There are over 17 million golfers in the $75,000+ annual income bracket, outnumbering sailors, skiers, tennis players, and runners. Devoted golfers, those who play 25 or more rounds per year, are more likely to be a male age 25 to 34 or over 65, be married, own a vacation home, and hold a graduate degree.

Soar with the Eagles...Play the Mountain

The 18-hole semi-private facility offers five sets of tees ranging from 5,000 to 7,000 yards, making the course suitable and attractive for golfers of all skill levels. The course features white sand bunkers, Empire Zoysia fairways, and SR 1119 Bentgrass greens. Numerous water hazards, lakes, abundant wildlife, and the beautiful White River make for a spectacular backdrop.

Mountain Ridge Estates was developed in conjunction with The Course at Eagle Mountain. The Estates feature 200 residences on approximately 500 acres overlooking the river and the golf course. Eagle Mountain Realty is located on-site, with lot prices beginning at $40,000.

By 2008, investment in the facility was complete. The owners are determined to make the development one of the premier residential communities in North Arkansas.

Questions:

1. What factors affect the level of consumer involvement in the purchase decision in this marketplace?
2. What types of marketing research would help the owners better understand their potential customers?
3. Design a 10-question survey to help the owners better understand the needs and wants of potential customers.

PART 3

Product Decisions

WHAT'S INSIDE

COURTESY OF DELL, INC.

Product Concepts

CHAPTER
10

Learning Outcomes

LO 1 Define the term *product*

LO 2 Classify consumer products

LO 3 Define the terms *product item*, *product line*, and *product mix*

LO 4 Describe marketing uses of branding

LO 5 Describe marketing uses of packaging and labeling

LO 6 Discuss global issues in branding and packaging

LO 7 Describe how and why product warranties are important marketing tools

LO 1
What Is a Product?

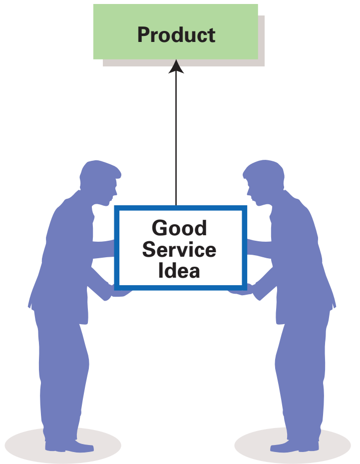
The product offering, the heart of an organization's marketing program, is usually the starting point in creating a marketing mix. A marketing manager cannot determine a price, design a promotion strategy, or create a distribution channel until the firm has a product to sell. Moreover, an excellent distribution channel, a persuasive promotion campaign, and a fair price are useless if the product offering is poor or inadequate.

A **product** may be defined as everything, both favorable and unfavorable, that a person receives in an exchange. A product may be a tangible good like a pair of shoes, a service like a haircut, an idea like "don't litter," or any combination of these three. Packaging, style, color, options, and size are some typical product features. Just as important are intangibles such as service, the seller's image, the manufacturer's reputation, and the way consumers believe others will view the product.

To most people, the term *product* means a tangible good. However, services and ideas are also products. (Chapter 12 focuses specifically on the unique aspects of marketing services.) The marketing process identified in Chapter 1 is the same whether the product marketed is a good, a service, an idea, or some combination of these.

REVIEW LEARNING OUTCOME

LO 1 Define the term *product*



Marketing & You

Using the following scale, indicate your opinion on the line before each item.

1	2	3	4	5
Strongly disagree	Disagree	Neutral	Agree	Strongly agree

— I usually purchase brand-name products.

— Store brands are of poor quality.*

— All brands are about the same.*

— The well-known national brands are best for me.

— I usually choose more expensive brands.

— The higher a product's price, the better its quality.

— Nice department and specialty stores offer me the best products.

Total your score, reversing your scores for the items followed by an asterisk. That is, if you answered 1, change it to 5 and vice versa. Read the chapter and find out what your score means at the end.

LO 2
Types of Consumer Products

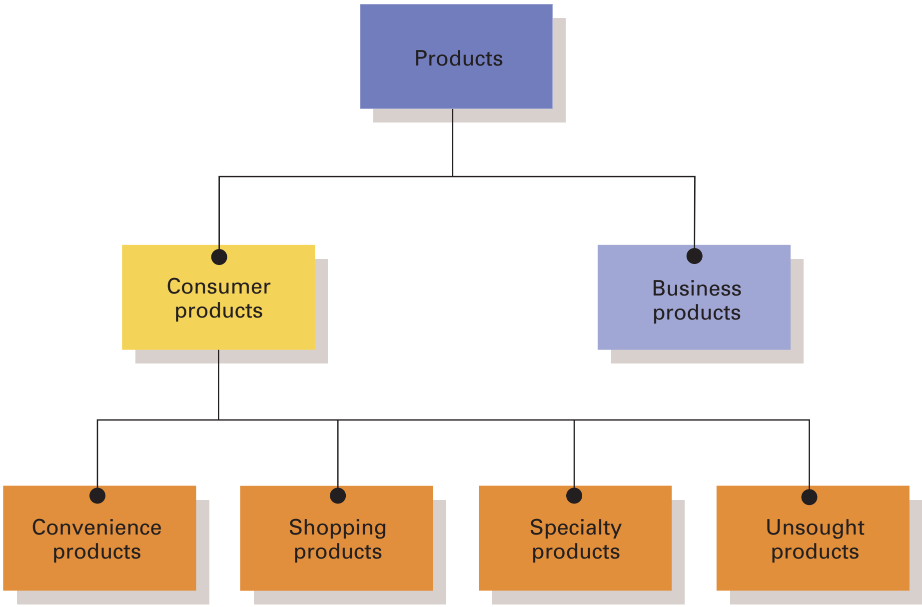
product
Everything, both favorable and unfavorable, that a person receives in an exchange.

business product (industrial product)
A product used to manufacture other goods or services, to facilitate an organization's operations, or to resell to other customers.

Products can be classified as either business (industrial) or consumer products, depending on the buyer's intentions. The key distinction between the two types of products is their intended use. If the intended use is a business purpose, the product is classified as a business or industrial product. As explained in Chapter 7, a **business product** is used

Exhibit 10.1

Classification of Consumer Products



to manufacture other goods or services, to facilitate an organization's operations, or to resell to other customers. A **consumer product** is bought to satisfy an individual's personal wants. Sometimes the same item can be classified as either a business or a consumer product, depending on its intended use. Examples include lightbulbs, pencils and paper, and computers.

We need to know about product classifications because business and consumer products are marketed differently. They are marketed to different target markets and tend to use different distribution, promotion, and pricing strategies.

Chapter 7 examined seven categories of business products: major equipment, accessory equipment, component parts, processed materials, raw materials, supplies, and services. The current chapter examines an effective way of categorizing consumer products. Although there are several ways to classify them, the most popular approach includes these four types: convenience products, shopping products, specialty products, and unsought products (see Exhibit 10.1). This approach classifies products according to how much effort is normally used to shop for them.

CONVENIENCE PRODUCTS

consumer product
A product bought to satisfy an individual's personal wants.

convenience product
A relatively inexpensive item that merits little shopping effort.

shopping product
A product that requires comparison shopping because it is usually more expensive than a convenience product and is found in fewer stores.

A **convenience product** is a relatively inexpensive item that merits little shopping effort—that is, a consumer is unwilling to shop extensively for such an item. Candy, soft drinks, combs, aspirin, small hardware items, dry cleaning, and car washes fall into the convenience product category.

Consumers buy convenience products regularly, usually without much planning. Nevertheless, consumers know the brand names of popular convenience products, like Coca-Cola, Bayer aspirin, and Right Guard deodorant. Convenience products normally require wide distribution in order to sell sufficient quantities to meet profit goals. For example, the gum Dentyne Ice is available everywhere, including Wal-Mart, Walgreens, Shell gas stations, newsstands, and vending machines.

© MARK STOKES/ISTOCKPHOTO INTERNATIONAL INC.

SHOPPING PRODUCTS

A **shopping product** is usually more expensive than a convenience product and found in fewer stores. Consumers usually buy a shopping product only after comparing several brands or stores in terms of style, practicality, price, and lifestyle compatibility. They are willing to invest some effort into this process to get the desired benefits.

There are two types of shopping products: homogeneous and heterogeneous. Consumers perceive *homogeneous* shopping products as essentially similar—for example, washers, dryers, refrigerators, and televisions. In choosing homogeneous shopping products, consumers typically look for the lowest-priced brand with the desired features. For example, they might compare Kenmore, Whirlpool, and General Electric refrigerators.

specialty product
A particular item for which consumers search extensively and are very reluctant to accept substitutes.

unsought product
A product unknown to the potential buyer, or a known product that the buyer does not actively seek.

product item
A specific version of a product that can be designated as a distinct offering among an organization's products.

product line
A group of closely related product items.

product mix
All products that an organization sells.

In contrast, consumers perceive *heterogeneous* shopping products as essentially different—for example, furniture, clothing, housing, and universities. Consumers often have trouble comparing heterogeneous shopping products because the prices, quality, and features vary so much. The goal of comparing heterogeneous shopping products is "finding the best product or brand for me"; this decision is often highly individual. For example, it would be difficult to compare a small, private college with a large, public university.

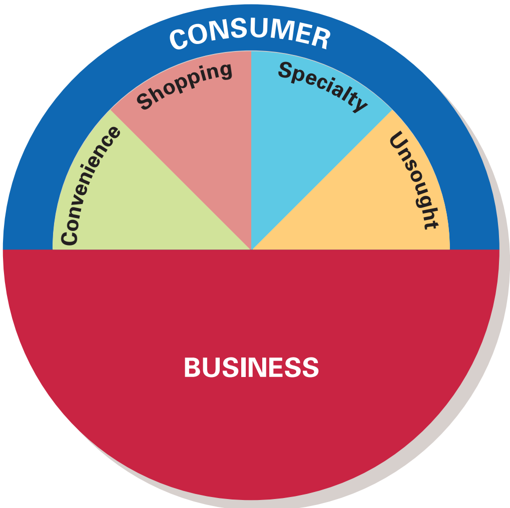
SPECIALTY PRODUCTS

When consumers search extensively for a particular item and are very reluctant to accept substitutes, that item is a specialty product. Rolex watches, Rolls Royce automobiles, Bose speakers, Ruth's Chris Steak House, and highly specialized forms of medical care are generally considered specialty products.

Marketers of specialty products often use selective, status-conscious advertising to maintain their product's exclusive image. Distribution is often limited to one or a very few outlets in a geographic area. Brand names and quality of service are often very important.

REVIEW LEARNING OUTCOME

LO 2 Classify consumer products



UNSOUGHT PRODUCTS

A product unknown to the potential buyer or a known product that the buyer does not actively seek is referred to as an unsought product. New products fall into this category until advertising and distribution increase consumer awareness of them.

Some goods are always marketed as unsought items, especially needed products we do not like to think about or care to spend money on. Insurance, burial plots, and similar items require aggressive personal selling and highly persuasive advertising. Salespeople actively seek leads to potential buyers. Because consumers usually do not seek out this type of product, the company must go directly to them through a salesperson, direct mail, or direct-response advertising.

LO 3 Product Items, Lines, and Mixes

Rarely does a company sell a single product. More often, it sells a variety of things. A product item is a specific version of a product that can be designated as a distinct offering among an organization's products. Campbell's Cream of Chicken soup is an example of a product item (see Exhibit 10.2).

A group of closely related product items is a product line. For example, the column in Exhibit 10.2 titled "Canned Soups" represents one of Campbell's product lines. Different container sizes and shapes also distinguish items in a product line. Diet Coke, for example, is available in cans and various plastic containers. Each size and each container are separate product items.

An organization's product mix includes all the products it sells. Together, all of Campbell's products—canned soups, microwave soups, gravies, meal kits and

Exhibit 10.2

Campbell's Product Lines and Product Mix

	Width Of The Product Mix				
Depth Of The Product Lines	Canned Soups	Microwave Soups	Gravies	Meal Kits	Tomato Juice
	Chicken Noodle	Creamy Tomato	Beef	Chicken Pasta	Regular
	Tomato	Vegetable	Turkey	Stroganoff Pasta	Low Sodium
	Vegetable Beef	Chicken Noodle	Mushroom	Chicken With Rice	Organic
	French Onion	Creamy Chicken	Chicken	Pork Chops With Stuffing	Healthy Request
	More	More	More	More	

SOURCE: Campbell's Web site: **http://www.campbellsoup.com**, June 10, 2008.

tomato juice—constitute its product mix. Each product item in the product mix may require a separate marketing strategy. In some cases, however, product lines and even entire product mixes share some marketing strategy components. Nike promotes all of its product items and lines with the theme "Just Do It."

Organizations derive several benefits from organizing related items into product lines, including the following:

- *Advertising economies:* Product lines provide economies of scale in advertising. Several products can be advertised under the umbrella of the line. Campbell's can call its soup "m-m-good" and promote the entire line.
- *Package uniformity:* A product line can benefit from package uniformity. All packages in the line may have a common look and still keep their individual identities. Again, Campbell's soup is a good example.
- *Standardized components:* Product lines allow firms to standardize components, thus reducing manufacturing and inventory costs. For example, many of the components Samsonite uses in its folding tables and chairs are also used in its patio furniture. General Motors uses the same parts on many automobile makes and models.
- *Efficient sales and distribution:* A product line enables sales personnel for companies like Procter & Gamble to provide customers with a full range of choices. Distributors and retailers are often more inclined to stock the company's products if it offers a full line. Transportation and warehousing costs are likely to be lower for a product line than for a collection of individual items.
- *Equivalent quality:* Purchasers usually expect and believe that all products in a line are of equal quality. Consumers expect that all Campbell's soups and all Mary Kay cosmetics will be of similar quality.

product mix width
The number of product lines an organization offers.

product line depth
The number of product items in a product line.

Product mix width (or breadth) refers to the number of product lines an organization offers. In Exhibit 10.2, for example, the width of Campbell's product mix is five product lines. **Product line depth** is the number of product items in a product line. As shown in Exhibit 10.2, the gravy product line includes several product items; the meal kits product line includes four product items.

Firms increase the *width* of their product mix to diversify risk. To generate sales and boost profits, firms spread risk across many product lines instead of depending on only one or two. Firms also widen their product mix to capitalize on established reputations. The Oreo Cookie brand was extended to include items such as breakfast cereal, ice cream, Jell-O pudding, and cake mix.

Firms increase the *depth* of their product lines to attract buyers with different preferences, to increase sales and profits by further segmenting the market, to capitalize on economies of scale in production and marketing, and to even out seasonal sales patterns. Procter & Gamble added some lower-priced versions of its

Oral-B's Stages toothbrushes represent a functional modification to adult toothbrushes. Numerous colors and designs of a single-stage toothbrush would be a style modification.

namesake brands, including Bounty Basic and Charmin Basic. These brands target more price-sensitive customers, a segment that P&G had not served with its more premium brands.[1] As another example, Oreo Cookies come in a variety of flavors, including Double Delight Mint Creme, Chocolate Creme, Uh-Oh Oreos (vanilla cookie, chocolate filling), and Double Delight Peanut Butter and Chocolate.

ADJUSTMENTS TO PRODUCT ITEMS, LINES, AND MIXES

Over time, firms change product items, lines, and mixes to take advantage of new technical or product developments or to respond to changes in the environment. They may adjust by modifying products, repositioning products, or extending or contracting product lines.

Product Modification

Marketing managers must decide if and when to modify existing products. Product modification changes one or more of a product's characteristics:

- *Quality modification:* change in a product's dependability or durability. Reducing a product's quality may let the manufacturer lower the price and appeal to target markets unable to afford the original product. Conversely, improving quality can help the firm compete with rival firms. Improving quality can also result in increased brand loyalty, greater ability to raise prices, or new opportunities for market segmentation. Inexpensive inkjet printers have improved in quality enough to produce photo-quality images. These printers now compete with camera film. To appeal to a more upscale market, Robert Mondavi Winery introduced a high-end wine called Twin Oaks to prestigious restaurants and hotels. This wine is positioned as a higher-quality wine than the one Mondavi sells in supermarkets.
- *Functional modification:* change in a product's versatility, effectiveness, convenience, or safety. Tide with Downy combines the functions of detergent and fabric softening in one product. Lea & Perrins offers its steak sauce in a value-priced squeeze bottle with a "no mess, stay clean" cap.
- *Style modification:* aesthetic product change, rather than a quality or functional change. Procter & Gamble added Febreze scents to its Tide liquid laundry detergent, Downy liquid fabric softener, and Bounce dryer sheets. These products all promise their usual function, with a touch of scent to improve their aesthetics.[2] Clothing and auto manufacturers often use style modifications to motivate customers to replace products before they wear out. Planned obsolescence is a term commonly used to describe the practice of modifying products so that those that have already been sold become obsolete before they actually need replacement. For example, products like printers and cell phones become obsolete because technology changes so quickly. Some feel that planned obsolescence is wasteful; they claim it is unethical. Marketers argue that consumers favor style modifications because they like

product modification
Changing one or more of a product's characteristics.

planned obsolescence
The practice of modifying products so those that have already been sold become obsolete before they actually need replacement.

changes in the appearance of goods such as clothing and cars. Marketers also contend that consumers, not manufacturers and marketers, decide when styles are obsolete.

Repositioning

Repositioning, as Chapter 8 explained, involves changing consumers' perceptions of a brand. A promotion by the Diamond Trading Company, a division of De Beers, encouraged women to buy their own "right-hand" diamonds. The company wanted to reposition its diamond rings as expressions of women's individuality and style, rather than symbols of love and commitment.[3]

© VICKI BEAVER

Changing demographics, declining sales, and changes in the social environment often motivate firms to reposition established brands. The clothing retailer Banana Republic started out selling safari-style clothing, but the concept soon became outdated. Gap acquired the chain and repositioned it as an upscale retailer of casual business clothing. Research told Hormel that consumers ages 18 to 35 were familiar with the Spam brand, but were put off by the inconvenience and negative image of the can it traditionally came in. In response, Hormel packaged single slices of Spam in a high-tech foil poch in an effort to appeal to these active young consumers.[4]

Product Line Extensions

A product line extension occurs when a company's management adds products to an existing product line in order to compete more broadly in the industry. Proctor & Gamble extended its Febreze odor freshener line with Febreze to Go aimed at travelers.[5] Kraft extended a number of its popular Nabisco brands by adding small-portioned, 100-calorie packages, targeting people with active lifestyles. PepsiCo added Aquafina Alive, a low-calorie, fruit-flavored, vitamin-enhanced water to continue being competitive in the bottled water market.[6]

product line extension
Adding additional products to an existing product line in order to compete more broadly in the industry.

brand
A name, term, symbol, design, or combination thereof that identifies a seller's products and differentiates them from competitors' products.

brand name
That part of a brand that can be spoken, including letters, words, and numbers.

brand mark
The elements of a brand that cannot be spoken.

brand equity
The value of company and brand names.

global brand
A brand where at least one-third of the product is sold outside its home country or region.

Product Line Contraction

Does the world really need 31 varieties of Head and Shoulders shampoo? Or 52 versions of Crest? Or numerous brands of apparel? Limited Brands once offered trendy apparel to several segments of the market. The company has now divested itself of nearly all its apparel stores, choosing to focus on its faster growing Victoria's Secret and Bath and Body Works chains.[7] Symptoms of product line overextension include the following:

- Some products in the line do not contribute to profits because of low sales or because they cannibalize sales of other items in the line.
- Manufacturing or marketing resources are disproportionately allocated to slow-moving products.
- Some items in the line are obsolete because of new product entries in the line or new products offered by competitors.

Firms contracting overextended product lines can expect three major benefits. First, contraction concentrates resources on the most important products. Second, managers no longer waste resources trying to improve the sales and profits of poorly performing products. Third, new product items have a greater chance of succeeding because more financial and human resources are available to manage them.

REVIEW LEARNING OUTCOME

LO3 Define the terms *product item, product line* and *product mix*

PRODUCT MIX WIDTH (6 wide)

PRODUCT LINES	STUDIO ENTERTAINMENT	PARKS & RESORTS	MEDIA CABLE	MEDIA BROADCAST	MEDIA INTERNET	CONSUMER PRODUCTS
DEPTH	Walt Disney Pictures Walt Disney Feature Animation DisneyToon Studio Touchstone Miramax Buena Vista Pixar (7 deep)	Disneyland Disney World Epcot Disneyland Tokyo Disneyland Cruiseline Disney Vacation Club Euro Disney → Repositioned as Disneyland Paris	Disney ESPN ABC Family E! Lifetime SOAPNET A&E The History Channel	ABC Touchstone TV	~~"GO" portal~~ → Product line contraction	Movie merchandise Disney Publishing Toys Apparel Games Baby Einstein → Product line extension

LO4 Branding

The success of any business or consumer product depends in part on the target market's ability to distinguish one product from another. Branding is the main tool marketers use to distinguish their products from the competition's.

A brand is a name, term, symbol, design, or combination thereof that identifies a seller's products and differentiates them from competitors' products. A brand name is that part of a brand that can be spoken, including letters (GM, YMCA), words (Chevrolet), and numbers (WD-40, 7-Eleven). The elements of a brand that cannot be spoken are called the brand mark—for example, the well-known Mercedes-Benz and Delta Air Lines symbols.

PR NEWSFOTO/© 7-ELEVEN

7-Eleven, Inc. was the very first convenience store open "around the clock".

BENEFITS OF BRANDING

Branding has three main purposes: product identification, repeat sales, and new-product sales. The most important purpose is *product identification*. Branding allows marketers to distinguish their products from all others. Many brand names are familiar to consumers and indicate quality.

The term brand equity refers to the value of company and brand names. A brand with high awareness, perceived quality, and brand loyalty among customers has high brand equity. Starbucks, Volvo, and Dell are companies with high brand equity. A brand with strong brand equity is a valuable asset.

The term global brand refers to a brand that obtains at least a third of its earnings from outside its

© CB2

Crate and Barrel established CB2 to appeal to urban consumers. This advertisement identifies the new brand as a supplier of modern furniture and accesories.

home country, is recognizable outside its home base of customers, and has publicly available marketing and financial data.[8] Exhibit 10.3 lists the top ten global brands. Yum! Brands, which owns Pizza Hut, KFC, and Taco Bell, is a good example of a company that has developed strong global brands. Yum believes that it has to adapt its restaurants to local tastes and different cultural and political climates. In Japan, for instance, KFC sells tempura crispy strips. In northern England, KFC serves gravy and potatoes, and in Thailand it offers rice with soy or sweet chili sauce.

The best generators of *repeat sales* are satisfied customers. Branding helps consumers identify products they wish to buy again and avoid those they do not. Brand loyalty, a consistent preference for one brand over all others, is quite high in some product categories. Over half the users in product categories such as cigarettes, mayonnaise, toothpaste, coffee, headache remedies, photographic film, bath soap, and ketchup are loyal to one brand. Many students come to college and purchase the same brands they used at home, rather than being "price" buyers. Brand identity is essential to developing brand loyalty.

The third main purpose of branding is to *facilitate new-product sales*. Company and brand names like those listed in Exhibit 10.3 are extremely useful when introducing new products.

The Internet provides firms with a new venue for generating brand awareness, promoting a desired brand image, stimulating new and repeat brand sales, enhancing brand loyalty, and building brand equity. Nearly all packaged-goods firms have a presence online. Tide.com offers a useful feature called Stain Detective, a digital tip sheet on removing almost any substance from almost any fabric.

brand loyalty
A consistent preference for one brand over all others.

generic product
A no-frills, no-brand-name, low-cost product that is simply identified by its product category.

BRANDING STRATEGIES

Firms face complex branding decisions. As Exhibit 10.4 illustrates, the first decision is whether to brand at all. Some firms actually use lack of a brand name as a selling point. These unbranded products are called generic products. Firms that decide to brand their products may choose to follow a policy of using manufacturers' brands, private (distributor) brands, or both. In either case, they must then decide among a policy of individual branding (different brands for different products), family branding (common names for different products), or a combination of individual branding and family branding.

Exhibit 10.3
The Top Ten Global Brands

Global
1. Coca Cola
2. Microsoft
3. IBM
4. GE
5. Nokia
6. Toyota
7. Intel
8. McDonald's
9. Disney
10. Mercedes-Benz

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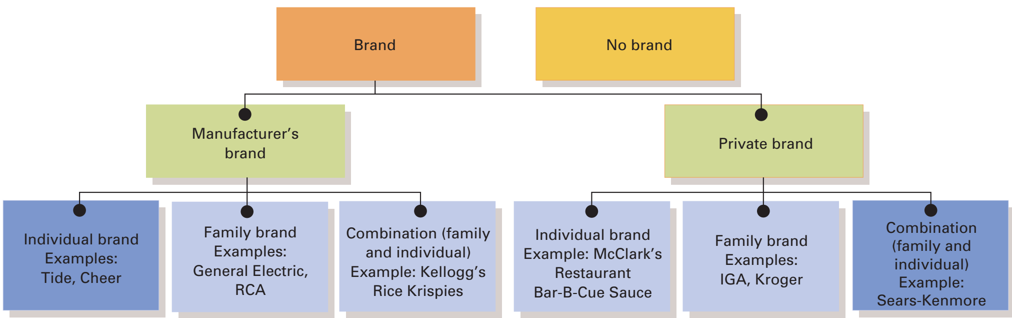
Generic Products versus Branded Products

A generic product is typically a no-frills, no-brand-name, low-cost product that is simply identified by its product category. (Note that a generic product and a brand name that becomes generic, such as cellophane, are not the same thing.)

The main appeal of generics is their low price. Generic grocery products are usually 30 to 40 percent less expensive than manufacturers' brands in the same

Exhibit 10.4
Major Branding Decisions



COURTESY OF HEINEKEN INTERNATIONAL

Heineken is trying to do for its beer what Starbucks has done for its coffee—create a social "brand experience." To this end, Heineken, Europe's largest beer brewer, has partnered with airport food-and-beverage operators to create a chain of Heineken bars in airports worldwide.

product category and 20 to 25 percent less expensive than retailer-owned brands.

Generics have made serious inroads in the pharmaceutical product category. When patents on successful pharmaceutical products expire, low-cost generics rapidly appear on the market. For example, when the patent on Merck's popular anti-arthritis drug Clinoril expired, sales declined by 50 percent almost immediately.

Manufacturers' Brands versus Private Brands

The brand name of a manufacturer—such as Kodak, La-Z-Boy, and Fruit of the Loom—is called a **manufacturer's brand.** Sometimes "national brand" is used as a synonym for "manufacturer's brand." This term is not always accurate, however, because many manufacturers serve only regional markets. Using "manufacturer's brand" more precisely defines the brand's owner.

A **private brand,** also known as a private label or store brand, is a brand name owned by a wholesaler or a retailer. Private brands include Wal-Mart's Ol' Roy dog food, which has surpassed Nestlé's Purina as the world's top-selling dog food, and the George line of apparel, which has knocked Liz Claiborne's clothing out of Wal-Mart. Private labels and products made exclusively by retailers account for one of every five items sold in the United States and represent over $50 billion in annual sales.[9] A survey conducted for the Private Manufacturers' Label Association found that 41 percent of shoppers identify themselves as frequent buyers of store brands, and 7 out of ten feel the private-label products they buy are as good as, if not better than, their national brand counterparts.[10] At JCPenney, 40 percent of sales come from private-label brands.[11] Staples adds several hundred private-branded products every year; in 2004, they accounted for 15 percent of the company's sales. Staples is unusual in that it is developing its own products rather than just putting its name on existing ones.[12]

manufacturer's brand
The brand name of a manufacturer.

private brand
A brand name owned by a wholesaler or a retailer.

Retailers love consumers' increased acceptance of private brands. Because overhead is low and there are no marketing costs, private-label products bring 10 percent higher margins, on average, than manufacturers' brands. More than that, a trusted store brand can differentiate a chain from its competitors. For example, many shoppers will drive the extra mile to Costco, a wholesale club, to buy the store's Kirkland brands and will also buy other goods while they are there. Costco has recently introduced a Kirkland Signature brand of wines that compete at the premium and super premium price categories.[13] Exhibit 10.5 illustrates key issues that wholesalers and retailers should consider in deciding whether to sell manufacturers' brands or private brands. Many firms offer a combination of both. Competition from private brands is forcing some manufacturers' brands to protect their trademarks and brand equity more aggressively. In the first quarter of 2006, Procter & Gamble filed four lawsuits against various private-label companies, accusing them of trademark infringement, false advertising, and unfair competition. P&G claims the companies have been knocking off the packaging of popular P&G brands, like Pantene, Head and Shoulders, and Crest, which each generate over $1 billion in annual sales for P&G. With U.S. consumer spending on private-label personal care products growing faster than sales of private-label food and beverage, it's no wonder that P&G is responding vigorously to private brands that knock off its successful brands.[14]

Exhibit 10.5

Comparing Manufacturers' and Private Brands from the Reseller's Perspective

Key Advantages of Carrying Manufacturers' Brands	Key Advantages of Carrying Private Brands
• Heavy advertising to the consumer by manufacturers like Procter & Gamble helps develop strong consumer loyalties.	• A wholesaler or retailer can usually earn higher profits on its own brand. In addition, because the private brand is exclusive, there is less pressure to mark the price down to meet competition.
• Well-known manufacturers' brands, such as Kodak and Fisher-Price, can attract new customers and enhance the dealer's (wholesaler's or retailer's) prestige.	• A manufacturer can decide to drop a brand or a reseller at any time or even to become a direct competitor to its dealers.
• Many manufacturers offer rapid delivery, enabling the dealer to carry less inventory.	• A private brand ties the customer to the wholesaler or retailer. A person who wants a Die-Hard battery must go to Sears.
• If a dealer happens to sell a manufacturer's brand of poor quality, the customer may simply switch brands and remain loyal to the dealer.	• Wholesalers and retailers have no control over the intensity of distribution of manufacturers' brands. Wal-Mart store managers don't have to worry about competing with other sellers of Sam's American Choice products or Ol' Roy dog food. They know that these brands are sold only in Wal-Mart and Sam's Wholesale Club stores.

Individual Brands versus Family Brands

Many companies use different brand names for different products, a practice referred to as **individual branding**. Companies use individual brands when their products vary greatly in use or performance. For instance, it would not make sense to use the same brand name for a pair of dress socks and a baseball bat. Procter & Gamble targets different segments of the laundry detergent market with Bold, Cheer, Dash, Dreft, Era, Gain, Ivory Snow, and Tide. Marriott International also targets different market segments with Courtyard by Marriott, Residence Inn, and Fairfield Inn.

individual branding
Using different brand names for different products.

family brand
Marketing several different products under the same brand name.

cobranding
Placing two or more brand names on a product or its package.

In contrast, a company that markets several different products under the same brand name is using a family brand. Sony's **family brand** includes radios, television sets, stereos, and other electronic products. A brand name can only be stretched so far, however. Do you know the differences among Holiday Inn, Holiday Inn Express, Holiday Inn Select, Holiday Inn Sunspree Resort, Holiday Inn Garden Court, and Holiday Inn Hotel & Suites? Most travelers don't.

Cobranding

Cobranding entails placing two or more brand names on a product or its package. Three common types of cobranding are ingredient branding, cooperative branding, and complementary branding. *Ingredient branding* identifies the brand of a part that makes up the product. Examples of ingredient branding are Intel (a microprocessor) in a personal computer, such as Dell, or a satellite system (OnStar) in an automobile (Cadillac). *Cooperative branding* occurs when two brands receiving equal treatment (in the context of an advertisement) borrow from each other's brand equity. A promotional contest jointly sponsored by Ramada Inns, American Express, and Continental Airlines is an example of cooperative branding. Guests at Ramada who paid with an American Express card were automatically entered in the contest and were eligible to win more than a hundred getaways for two at any Ramada in the continental United States and round-trip airfare from Continental. Finally, with *complementary branding*, products are advertised or marketed together to suggest usage, such as a spirits brand (Seagram's) and a compatible mixer (7-Up).

© AP PHOTO

This image, featuring both Nike and Apple products, illustrates an example of cobranding. Cobranding is a useful strategy when a combination of brand names enhances the prestige or perceived value of a product.

Cobranding is a useful strategy when a combination of brand names enhances the prestige or perceived value of a product, or when it benefits brand owners and users. When Intel launched its Centrino

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When FedEx purchased Kinko's in 2004, it merged the company's brand names to make one brand entity in the mind of the consumer. In late 2008, having successfully cobranded a shipping business and a copy/print/data center business, the company plans to rename the brand "Fedex Office."

wireless processor, it established cobranding relationships with T-Mobile and hotel chains Marriott International and Westin Hotels & Resorts because there was mutual value in doing so. T-Mobile was able to set up global "hot spots" to reach Intel's target market of mobile professionals, while the hotel chains enabled Intel to target business professionals.[15] Yum! Brands leads in volume for retail franchise cobranding concepts. This company has a mix of KFCs and Taco Bells, KFCs and A&Ws, Taco Bells and Long John Silver's, and Pizza Huts and WingStreets.[16]

Cobranding may be used to increase a company's presence in markets where it has little or no market share. For example, Coach was able to build a presence in a whole new category when its logo appeared on leather upholstery in Lexus automobiles.[17]

European firms have been slower to adopt cobranding than U.S. firms have. One reason is that European customers seem to be more skeptical than U.S. customers about trying new brands. European retailers also typically have less shelf space than their U.S. counterparts and are less willing to try new brands.

TRADEMARKS

A trademark is the exclusive right to use a brand or part of a brand. Others are prohibited from using the brand without permission. A service mark performs the same function for services, such as H&R Block and Weight Watchers. Parts of a brand or other product identification may qualify for trademark protection. Some examples are

- Shapes, like the Jeep front grille and the Coca-Cola bottle
- Ornamental color or design, such as the symbol on Nike tennis shoes, the black-and-copper color combination of a Duracell battery, Levi's small tag on the left side of the rear pocket of its jeans, or the cutoff black cone on the top of Cross pens
- Catchy phrases, such as Prudential's "Own a piece of the rock," Mountain Dew's "Do the Dew," and Nike's "Just Do It!"
- Abbreviations, such as Bud, Coke, or The Met
- Sounds, like General Electric Broadcasting Company's ship's bell clock sound and the MGM lion's roar.

It is important to understand that trademark rights come from use rather than registration. A company must have a genuine intention to use a trademark when it files an intent-to-use application with the U.S. Patent and Trademark Office and must actually use the mark within three years of the application being granted. Trademark protection lasts for as long as the mark is being used.

Legislation applying trademark law to the online world went into effect in November 1999. This law includes financial penalties for those who violate trademarked products or register an otherwise trademarked term as a domain name.

Companies that fail to protect their trademarks face the possibility that their product names will become generic. A generic product name identifies a product by class or type and cannot be trademarked. Former brand names that were not sufficiently protected by their owners and were subsequently declared to be generic product names by U.S. courts include aspirin, cellophane, linoleum, thermos, kerosene, monopoly, cola, and shredded wheat.

trademark
The exclusive right to use a brand or part of a brand.

service mark
A trademark for a service.

generic product name
Identifies a product by class or type and cannot be trademarked.

Companies like Rolls Royce, Cross, Xerox, Levi Strauss, Frigidaire, and McDonald's aggressively enforce their trademarks. Rolls Royce, Coca-Cola, and Xerox even run newspaper and magazine ads stating that their names are trademarks and should not be used as descriptive or generic terms. Some ads threaten lawsuits against competitors that violate trademarks.

Despite severe penalties for trademark violations, trademark infringement lawsuits are not uncommon. One of the major battles is over brand names that closely resemble another brand name. Donna Karan filed a lawsuit against Donnkenny, Inc., whose Nasdaq trading symbol—DNKY—was too close to Karan's DKNY trademark.

Companies must also contend with fake or unauthorized brands, including fake Levi's jeans, Microsoft software, Rolex watches, Reebok and Nike footwear, and Louis Vuitton handbags. Knockoffs of Burberry's trademarked tan, black, white, and red plaid are easy to find in cheap shops all over the world, and loose imitations are found in some reputable department stores as well. One Web site sells a line of plaid bags, hats, and shoes that it claims are "inspired by Burberry." Burberry says it spends a couple million pounds each year running ads in trade publications and sending letters to trade groups, textile manufacturers, and retailers reminding them about its trademark rights. It also works with customs officials and local law enforcement to seize fakes, sues infringers, and scans the Internet for online chatter about counterfeits.[18]

In Europe, you can sue counterfeiters only if your brand, logo, or trademark is formally registered. Until recently, formal registration was required in each country in which a company sought protection. A company can now register its trademark in all European Union (EU) member countries with one application.

REVIEW LEARNING OUTCOME

LO4 Describe marketing uses of branding

Brand name: MGM

Brand mark:

COURTESY OF METRO GOLDWYN MAYER

BRANDING

Benefits

- Brand equity (from product identfication)
- Brand loyalty (from repeat sales)
- Brand recognition (to generate new product sales)

Strategies

Generic / Brand / Trademark → Manufacturer (Individual, Family, Combination); Private

LO5 Packaging

Packages have always served a practical function—that is, they hold contents together and protect goods as they move through the distribution channel. Today, however, packaging also promotes products and makes them easier and safer to use.

PACKAGING FUNCTIONS

The three most important functions of packaging are to contain and protect products, to promote products, and to facilitate the storage, use, and convenience of products. A fourth function of packaging that is becoming increasingly important is to facilitate recycling and reduce environmental damage.

Containing and Protecting Products

The most obvious function of packaging is to contain products that are liquid, granular, or otherwise divisible. Packaging also enables manufacturers, wholesalers, and retailers to market products in specific quantities, such as ounces.

Physical protection is another obvious function of packaging. Most products are handled several times between the time they are manufactured, harvested, or otherwise produced and the time they are consumed or used. Many products are shipped, stored, and inspected several times between production and consumption. Some, like milk, need to be refrigerated. Others, like beer, are sensitive to light. Still others, like medicines and bandages, must be kept sterile. Packages protect products from breakage, evaporation, spillage, spoilage, light, heat, cold, infestation, and many other conditions.

Promoting Products

Packaging does more than identify the brand, list the ingredients, specify features, and give directions. A package differentiates a product from competing products and may associate a new product with a family of other products from the same manufacturer. Welch's repackaged its line of grape juice–based jams, jellies, and juices to unify the line and get more impact on the shelf.

Packages use designs, colors, shapes, and materials to influence consumers' perceptions and buying behavior. For example, marketing research shows that health-conscious consumers are likely to think that any food is probably good for them so long as it comes in green packaging. Two top brands of low-fat foods—SnackWell's and Healthy Choice—use green packaging. Packaging can also influence consumers' perceptions of quality and/or prestige. Nestlé uses gold packaging to signal limited-edition flavors for some items in its Signature Treasures line of gourmet candy.[19]

Packaging has a measurable effect on sales. Quaker Oats revised the package for Rice-a-Roni without making any other changes in marketing strategy and experienced a 44 percent increase in sales in one year.

Facilitating Storage, Use, and Convenience

Wholesalers and retailers prefer packages that are easy to ship, store, and stock on shelves. They also like packages that protect products, prevent spoilage or breakage, and extend the product's shelf life.

Consumers' requirements for storage, use, and convenience cover many dimensions. Consumers constantly seek items that are easy to handle, open, and reclose; others want packages that are tamperproof or childproof. Research indicates that hard-to-open packages are among consumers' top complaints.[20] Surveys conducted by *Sales & Marketing Management* magazine revealed that consumers dislike—and avoid buying—leaky ice cream boxes, overly heavy or fat vinegar bottles, immovable pry-up lids on glass bottles, key-opener sardine cans, and hard-to-pour cereal boxes. Such packaging innovations as zipper tear strips, hinged lids, tab slots, screw-on tops, and pour spouts were introduced to solve these and other problems. Nestlé is trying to improve all its packaging to make it easier for people to rip open its pouches, twist off its caps, and reseal its tubs. Easy openings are especially important for kids and aging baby boomers. The company's package designers spent nine months developing a plastic lid for ice cream that pulls off easily when the ice cream is frozen and ribbed corners for ice cream cartons that are easier to grip while scooping.[21]

Some firms use packaging to segment markets. For example, a C&H sugar carton with an easy-to-pour, reclosable top is targeted to consumers who don't do much baking and are willing to pay at least 20 cents more for the package. Different-size packages appeal to heavy, moderate, and light users. Salt is sold in package sizes ranging from single serving to picnic size to giant economy size. Campbell's soup is packaged in single-serving cans aimed at the elderly and singles market segments. Beer and soft drinks are similarly marketed in various package sizes and types. Packaging convenience can increase a product's utility and, therefore, its

Image not available due to copyright restrictions

market share and profits. To appeal to women, Dutch Boy designed a square plastic paint container with a side handle and a spout to replace the traditional wire-handled round metal paint can. Women make up a large part of the interior paint customer base, thanks to popular do-it-yourself television programs, such as *Decorating Cents* and *Trading Spaces*.

The Internet will soon give consumers more packaging options. Indeed, the Internet may significantly change the purpose and appearance of packaging. Packaging for products sold on the Internet will be under greater customer control and often customized by consumers to fit their needs. Some designers are already offering to personalize, for a fee, packages like wine bottle labels.

Facilitating Recycling and Reducing Environmental Damage

One of the most important packaging issues today is environmental awareness. Some firms use their packaging to target environmentally concerned market segments. Target switched its packaging for iPod carrying cases from PVC, which has health and environmental risks, to eco-friendly cardboard.[22] Procter & Gamble markets Sure Pro and Old Spice in "eco-friendly" pump-spray packages that don't rely on aerosol propellants. Groups like the Sustainable Packaging Coalition help companies create perpetually recycled packaging so that materials don't ever end up in landfills, damaging the ecosystem.[23]

LABELING

An integral part of any package is its label. Labeling generally takes one of two forms: persuasive or informational. Persuasive labeling focuses on a promotional theme or logo, and consumer

ETHICS in Marketing

Organic—or Not?

Anheuser-Busch brand Wild Hop Lager has a USDA Organic seal stamped on its label, and is promoted as "the perfect organic experience." The Wild Hop Web site says "In today's world of artificial flavors, preservatives and factory farming, knowing what goes into what you eat can just about drive you crazy." However, the beer is made from hops grown with chemical fertilizers and sprayed with pesticides.

Sales of organic food in the U.S. more than doubled between 2002 and 2007 as consumers demanded products that are healthier for them and better for the environment. As big companies enter the organic market, which was formerly dominated by small businesses, questions about what goes into organic food have been raised.

The U.S. Department of Agriculture (USDA) proposed a rule change that would allow 38 nonorganic ingredients—including hops—to be used in organic foods. Food products made with up to 5 percent of these ingredients could be labeled "USDA Organic." Many types of manufactured food could be affected because these ingredients include widely used things like spices, colorings, and flavorings. In the case of beer, hops is a major flavoring, but it makes up less than 5 percent of the final product because beer is mostly water. Organic food proponents want to block all or parts of the new rule, arguing that it would allow food makers to mislead consumers. Carl Chamberlain, a research assistant with the Pesticide Education Project in Raleigh, North Carolina, claims that adding the 38 ingredients is a major blow to the organic movement in the U. S. because it could erode consumer confidence in organic standards.

Organic beer has been growing faster than overall organic food sales. An Anheuser-Busch spokesperson says that they can't find enough purely organic hops. However, Russell Klisch, owner of Milwaukee's Lakefront Brewery argues that his company has been brewing beer with 100 percent organic hops since 1996. He says there are enough organic hops to satisfy 90 percent of the current organic beer demand in the U.S., but that some brewers don't want to pay the higher prices organic hops command.[25]

Do you think the organic claim made by Wild Hop Lager is misleading consumers? Why or why not? What should the USDA standards be for allowing a manufacturer to put "organic" on a product label?

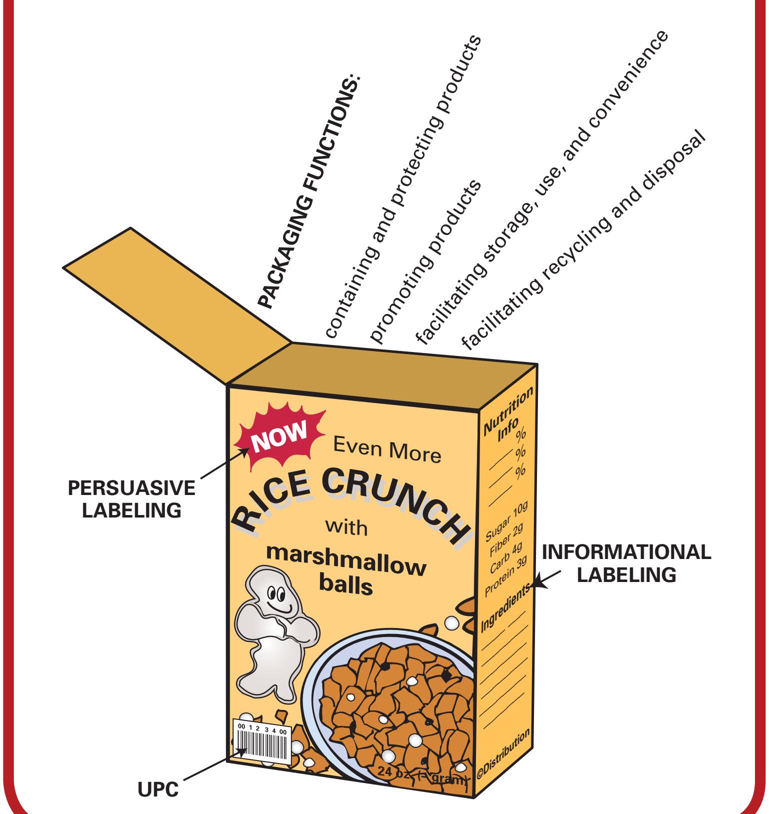
persuasive labeling
A type of package labeling that focuses on a promotional theme or logo with consumer information being secondary.

information is secondary. Procter & Gamble put real photography on its new Downy fabric softener labels to make a more personal connection with consumers.[24] Note that the standard promotional claims—such as "new," "improved," and "super"—are no longer very persuasive. Consumers have been saturated with "newness" and generally discount these claims.

Informational labeling, in contrast, is designed to help consumers make proper product selections and lower their cognitive dissonance after the purchase. Sears attaches a "label of confidence" to all its floor coverings. This label gives such product information as durability, color, features, cleanability, care instructions, and construction standards. Most major furniture manufacturers affix labels to their wares that explain the products' construction features, including type of frame, number of coils, and fabric characteristics. The Nutritional Labeling and Education Act of 1990 mandated detailed nutritional information be placed on most food packages and standards for health claims on food packaging. An important outcome of this legislation has been guidelines from the Food and Drug Administration for using terms like *low fat, light, reduced cholesterol, low sodium, low calorie*, and *fresh*.

REVIEW LEARNING OUTCOME

LO5 Describe marketing uses of packaging and labeling



UNIVERSAL PRODUCT CODES

The universal product codes (UPCs) that appear on most items in supermarkets and other high-volume outlets were first introduced in 1974. Because the numerical codes appear as a series of thick and thin vertical lines, they are often called *bar codes*. The lines are read by computerized optical scanners that match codes with brand names, package sizes, and prices. They also print information on cash register tapes and help retailers rapidly and accurately prepare records of customer purchases, control inventories, and track sales. The UPC system and scanners are also used in single-source research (see Chapter 9).

LO6

Global Issues in Branding and Packaging

International marketers must address several concerns regarding branding and packaging.

informational labeling
A type of package labeling designed to help consumers make proper product selections and lower their cognitive dissonance after the purchase.

universal product codes (UPCs)
A series of thick and thin vertical lines (bar codes), readable by computerized optical scanners, that represent numbers used to track products.

BRANDING

When planning to enter a foreign market with an existing product, a firm has three options for handling the brand name:

- *One brand name everywhere:* This strategy is useful when the company markets mainly one product and the brand name does not have negative connotations in any local market. The Coca-Cola Company uses a one-brand-name strategy in 195 countries around the world. The advantages of a one-brand-name

PR NEWSFOTO/© ORION INFORMATION SERVICES

Hugo enjoys fame in more than 40 countries and is one of the strongest global brands in children's entertainment. Orion has the exclusive license to distribute Hugo in the U.S.

strategy are greater identification of the product from market to market and ease of coordinating promotion from market to market.

- *Adaptations and modifications:* A one-brand-name strategy is not possible when the name cannot be pronounced in the local language, when the brand name is owned by someone else, or when the brand name has a negative or vulgar connotation in the local language. The Iranian detergent "Barf," for example, might encounter some problems in the U.S. market.
- *Different brand names in different markets:* Local brand names are often used when translation or pronunciation problems occur, when the marketer wants the brand to appear to be a local brand, or when regulations require localization. Gillette's Silkience hair conditioner is called Soyance in France and Sientel in Italy. The adaptations were deemed to be more appealing in the local markets. Coca-Cola's Sprite brand had to be renamed Kin in Korea to satisfy a government prohibition on the unnecessary use of foreign words. Because of the feminine connotations of the word *diet*, the European version of Diet Coke is Coca Cola Light.[26]

PACKAGING

Three aspects of packaging that are especially important in international marketing are labeling, aesthetics, and climate considerations. The major *labeling* concern is properly translating ingredient, promotional, and instructional information on labels. In Eastern Europe, packages of Ariel detergent are printed in 14 languages. Packaging must be carefully designed to meet all local labeling requirements. Several years ago, an Italian judge ordered that all bottles of Coca-Cola be removed from retail shelves because the ingredients were not properly labeled. Labeling is also harder in countries like Belgium and Finland, which require it to be bilingual.

Package *aesthetics* may also require some attention. The key is to stay attuned to cultural traits in host countries. For example, colors may have different connotations. Red is associated with witchcraft in some countries, green may indicate danger, and white may symbolize death. Aesthetics also influence package size. Soft drinks are not sold in six-packs in countries that lack refrigeration. In some regions, products like detergent may be bought only in small quantities because of limited storage space. Other products, like cigarettes, may be bought in small quantities, and even single units, because of the low purchasing power of buyers.

On the other hand, simple visual elements of the brand, such as a symbol or logo, can be a standardizing element across products and countries. For example, in Mexico, Lay's potato chips are known as Sabritas, but the packaging carries the same brand mark and graphic elements as in the United States.[27]

Extreme *climates* and long-distance shipping necessitate sturdier and more durable packages for goods sold overseas. Spillage, spoilage, and breakage are all more important concerns when products are shipped long distances or frequently handled during shipping and storage. Packages may also have to ensure a longer product life if the time between production and consumption lengthens significantly.

REVIEW LEARNING OUTCOME

LO 6 Discuss global issues in branding and packaging

Branding choices:	Packaging considerations:
1 name	Labeling
Modify or adapt 1 name	Aesthetics
Different names in different markets	Climate

LO7
Product Warranties

warranty
A confirmation of the quality or performance of a good or service.

express warranty
A written guarantee.

implied warranty
An unwritten guarantee that the good or service is fit for the purpose for which it was sold.

Just as a package is designed to protect the product, a **warranty** protects the buyer and gives essential information about the product. A warranty confirms the quality or performance of a good or service. An **express warranty** is a written guarantee. Express warranties range from simple statements—such as "100 percent cotton" (a guarantee of quality) and "complete satisfaction guaranteed" (a statement of performance)—to extensive documents written in technical language. In contrast, an **implied warranty** is an unwritten guarantee that the good or service is fit for the purpose for which it was sold. All sales have an implied warranty under the Uniform Commercial Code.

Congress passed the Magnuson-Moss Warranty–Federal Trade Commission Improvement Act in 1975 to help consumers understand warranties and get action from manufacturers and dealers. A manufacturer that promises a full warranty must meet certain minimum standards, including repair "within a reasonable time and without charge" of any defects and replacement of the merchandise or a full refund if the product does not work "after a reasonable number of attempts" at repair. Any warranty that does not live up to this tough prescription must be "conspicuously" promoted as a limited warranty.

REVIEW LEARNING OUTCOME

LO6 Describe how and why product warranties are important marketing tools

Express warranty	=	written guarantee
Implied warranty	=	unwritten guarantee

50 < percentage of decline in sales of the anti-arthritis drug Clinoril when its patent expired

annuals sales of private label brands in the U.S. > **$50 billion**

3 < years within which a company must use a trademark once it has been granted

44 < percentage of increased sales that Quaker Oats experienced when it revised the Rice-a-Roni package

countries in which Coca-Cola uses its one-brand-name strategy > **195**

4 < categories of business products

30 < percent price difference between manufacturers' brands and generic products

percentage of shoppers who frequently buy store brands > **41**

$1 billion < annuals sales that Crest generates for Procter and Gamble

the extra cost of an easy-pour, reclosable carton of C&H sugar > **20 cents**

Review and Applications

LO1 **Define the term *product*.** A product is anything, desired or not, that a person or organization receives in an exchange. The basic goal of purchasing decisions is to receive the tangible and intangible benefits associated with a product. Tangible aspects include packaging, style, color, size, and features. Intangible qualities include service, the retailer's image, the manufacturer's reputation, and the social status associated with a product. An organization's product offering is the crucial element in any marketing mix.

TEAM

1.1 Form a team of four or five members. Have the team determine what the tangible and intangible benefits are for a computer, a tube of toothpaste, a beauty salon, and a dentist.

LO2 **Classify consumer products.** Consumer products are classified into four categories: convenience products, shopping products, specialty products, and unsought products. Convenience products are relatively inexpensive and require limited shopping effort. Shopping products are of two types: homogeneous and heterogeneous. Because of the similarity of homogeneous products, they are differentiated mainly by price and features. In contrast, heterogeneous products appeal to consumers because of their distinct characteristics. Specialty products possess unique benefits that are highly desirable to certain customers. Finally, unsought products are either new products or products that require aggressive selling because they are generally avoided or overlooked by consumers.

TEAM

2.1 Break into groups of four or five. Have the members of the group classify each of the following products into the category (convenience, shopping, specialty, unsought) that they think fits best from their perspective as consumers (i.e., if they were buying the product): Coca-Cola (brand), car stereo, winter coat, pair of shoes, life insurance, blue jeans, fast-food hamburgers, shampoo, canned vegetables, curtains.

2.2 Although major appliances, like washers and dryers, are usually considered homogeneous shopping products, the high-efficiency front-loaders that boast many more features than standard machines are gaining in popularity. Do you think high-efficiency technology is enough to make washers and dryers heterogeneous shopping products? Explain.

LO3

Define the terms *product item*, *product line*, and *product mix*. A product item is a specific version of a product that can be designated as a distinct offering among an organization's products. A product line is a group of closely related products offered by an organization. An organization's product mix includes all the products it sells. Product mix width refers to the number of product lines an organization offers. Product line depth is the number of product items in a product line. Firms modify existing products by changing their quality, functional characteristics, or style. Product line extension occurs when a firm adds new products to existing product lines.

WRITING

3.1 A local civic organization has asked you to give a luncheon presentation about planned obsolescence. Rather than pursuing a negative approach by talking about how businesses exploit customers through planned obsolescence, you have decided to talk about the benefits of producing products that do not last forever. Prepare a one-page outline of your presentation.

ONLINE

3.2 Go to Unilever's Web site at **http://www.unilever.com**. Can Unilever delete anything from its product lines? Visit the company's product category pages on its "Brands" Web page to see the number of existing products and new products planned. Write a proposal for contracting one of Unilever's product lines.

LO4

Describe marketing uses of branding. A brand is a name, term, or symbol that identifies and differentiates a firm's products. Established brands encourage customer loyalty and help new products succeed. Branding strategies require decisions about individual, family, manufacturers', and private brands.

WRITING

4.1 A local supermarket would like to introduce its own brand of paper goods (i.e., paper towels, facial tissue, etc.) to sell alongside its current inventory. The company has hired you to generate a report outlining the advantages and disadvantages of doing so. Write the report.

ONLINE

4.2 How does Hormel use its Web site (**http://www.hormel.com**) to promote its store brands? Is the site designed more to promote the company or its brands? Check out the Spam Web site at **http://www.spam.com**. How do you think Hormel is able to successfully sustain this often-mocked brand?

LO5

Describe marketing uses of packaging and labeling. Packaging has four functions: containing and protecting products; promoting products; facilitating product storage, use, and convenience; and facilitating recycling and reducing environmental damage. As a tool for promotion, packaging identifies the brand and its features. It also serves the critical function of differentiating a product from competing products and linking it with related products from the same manufacturer. The label is an integral part of the package, with persuasive and informational functions. In essence, the package is the marketer's last chance to influence buyers before they make a purchase decision.

WRITING

5.1 Find a product at home that has a distinctive package. Write a paragraph evaluating that package based on the four functions of packaging discussed in the chapter.

LO6

Discuss global issues in branding and packaging. In addition to brand piracy, international marketers must address a variety of concerns regarding branding and packaging, including choosing a brand-name policy, translating labels and meeting host-country labeling requirements, making packages aesthetically compatible with host-country cultures, and offering the sizes of packages preferred in host countries.

6.1 List the countries to which Levi Strauss & Co. markets through the Web site **http://www.levi.com**. How do the product offerings differ between the U.S. and European selections?

LO7

Describe how and why product warranties are important marketing tools. Product warranties are important tools because they offer consumers protection and help them gauge product quality.

7.1 Lands' End and L.L. Bean are renowned for their product guarantees. Find and read the exact wording of their guarantees on their Web sites (**http://www.landsend.com** and **http://www.llbean.com**). Do you think a company could successfully compete against either without offering the same guarantee?

Key Terms

Exercises

APPLICATION EXERCISE

What is your favorite brand of sandwich cookie? If you're like most Americans, chances are it's Oreo. In fact, Oreos are so popular that many people think Oreo was the original sandwich cookie. But they're wrong. Sunshine first marketed its Hydrox sandwich cookie in 1908. Hydrox thrived until 1912, when Nabisco (now part of Kraft) launched Oreo. With Nabisco's superior distribution and advertising, Hydrox was soon outmatched. By 1998, Hydrox sales totaled $16 million, while Oreo's revenues were at $374 million. Hydrox has been purchased by Keebler (subsequently purchased by Kellogg), whose elves are trying to give the cookie a major facelift. You are part of the Keebler team deciding what to do with the Hydrox brand.

Activities

1. Can you re-create Hydrox through a name change? What kind of brand name could go head-to-head with Oreo? (Most people unfamiliar with Hydrox think it is a cleaning product.) Make a list of three to five possibilities.
2. How can you package your renewed sandwich cookie to make it more attractive on the shelf than Oreo? What about package size? Draft a brief packaging plan for the new Hydrox (or whatever name you chose).
3. Can you modify the original formula to make something new and more competitive? Will a brand extension work here? Why or why not?

ETHICS EXERCISE

A product that a potential buyer knows about but is not actively seeking is called an unsought product. Is the marketing of unsought products unethical? Discuss your answer in terms of the AMA Statement of Ethics, found at **http://www.marketingpower.com**.

Case Study: Terracycle

TURNING WORM POOP INTO A PRODUCT

Environmentally friendly products have never been as hot as they are now, and the number of brands touting their "green" credentials has never been higher, but TerraCycle Plant Food may be the ultimate organic product to hit the market. A college student named Tom Szaky founded TerraCycle in 2003 after buddies from Canada, "where they have more liberal rules about growing certain plants," he says, taught him how to use worm droppings as cheap and eco-friendly fertilizer.

Szaky based his business model on recycling, starting with the trash that TerraCycle turns into compost and feeds to millions of red worms. The worm castings are then liquefied and put into previously used plastic water and soda bottles. Even the company's shipping cartons come from recycled materials.

TerraCycle's organic plant food hit the shelves in 2004 with labels boasting that it "Contains Liquefied Worm Poop!" It didn't take long for the products to take off. By 2006, the company had been named "The Coolest Little Start-Up in America" by *Inc.* magazine and had passed the $1 million mark in sales, growing as much as 300 percent from the previous year. They snagged shelf space in retail giants such as Target, Wal-Mart, and Home Depot.

Founder and president Tom Szaky liked to refer to his company as "the anti-Miracle-Gro." But the industry giant disagreed. It turns out that Scotts Miracle-Gro thought that, if anything, TerraCycle was encroaching too closely on the industry giant's territory. In March of 2007, Scotts sued Szaky's fledgling company for trademark infringement and for making "false claims" that its organic products are superior to synthetic versions.

Small companies can easily fold under the weight of such a lawsuit. Even if they win, the legal costs can cripple them. So TerraCycle took their case to the Internet with the blog **www.suedbyscotts.com**, hoping to stir public support and raise contributions for its legal fees.

"I knew there was no way I could out-lawyer Scotts," Tom Szaky says. "So as I thought about it, I wondered what core competency our company had that we could exploit. Guerrilla marketing seemed to be the obvious answer." He adds that they hope to get so much public support for their cause that Scotts will drop their suit.

The blog offers a comparison chart titled "David vs. Goliath" that illustrates the differences between the two companies. A photo of TerraCycle's modest headquarters behind a chain-link fence in New Jersey is contrasted with Scotts's grand, pillared entryway in Ohio. It lists TerraCycle's "CEO major perquisite" as "unlimited free worm poop," whereas Scotts's CEO enjoys "personal use of company-owned aircraft."

The blog also counters Scotts's claims that consumers might be confused by its "overly similar yellow and green packaging" by posting photographs of TerraCycle's wacky and unusual bottles in their variety of shapes and sizes beside Miracle-Gro's uniform and professional looking ones. Scotts is insisting that they change their labels, but TerraCycle's general counsel, Richard Ober Jr., says that changing packaging now would hurt their sales momentum. "There's the loss of customer recognition."

Su Lok, a Scotts spokesperson, argues that the blog is just one of TerraCycle's PR "tactics" and insists that none of their arguments has merit. "We've spent a lot of time building up brands that consumers trust," she says, "and we are going to protect those brands."

So far **www.suedbyscotts.com** has gained massive media attention, leading major newspapers and magazines to cover the story, and hundreds of bloggers to defend TerraCycle's cause. Although online donations have totaled less than $1,000 to date, overall company sales surged 122 percent within weeks of the blog's launch. And TerraCycle's main Web site, which averages about 1,000 visitors a day, spiked to as high as 13,000. They expect to bring in revenue highs approaching $5 million by the end of 2007.

Ira J. Levy, an intellectual property lawyer, warns that Scotts may have more to lose by pursuing TerraCycle than it's worth. "By pursuing a trade dress case," Levy says, "they can allow a small player to promote itself on the national stage. When word gets out that the mega-conglomerate is suing the little guy, you risk having bloggers launching boycotts, and the plaintiff ends up injuring his own business."

Which is precisely what Tom Szaky hopes will happen. The lawsuit isn't something he would have wanted to fight, he says, but it's a chance to generate buzz. "It's like *The Art of War*," he says. "You need to have a villain to be up against, and for us, that's Scotts."[28]

Questions

1. What type of consumer product is TerraCycle's plant food: convenience, shopping, specialty, or unsought? Why?
2. Go to **http://www.terracycle.net** and look at the types of products the company sells. Describe their product mix. How wide is it? Which basic product lines does it sell? How long are they?
3. Do you think that product line extension or product line contraction would make more sense for TerraCycle at this stage of the company's growth? Why?
4. How well do TerraCycle's bottles perform the four packaging functions discussed in this chapter? Go to **www.suedbyscotts.com** to see what TerraCycle's products look like compared to Miracle-Gro's. Do you think TerraCycle's package design distinguishes their products well enough from those of the industry giant, or are they similar enough to cause customer confusion?

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Company Clips

KODAK—REINVENTING THE BRAND

Unquestionably, Kodak is one of most recognized brands in the United States and the world. For over a century, Kodak was known as the company that brought the technology of photography into the everyday, aptly summed up in the tag line, "Celebrate the Moments of Your Life." Grocery stores, convenient stores, and camera stores contained aisles full of little yellow boxes of Kodak film in every possible speed. But after Kodak invented the digital camera, the company was faced with the challenge of leveraging the equity of its brand in a new competitive market—one that didn't include film.

Questions

1. Using Exhibit 10.1 as a guide, create a diagram that organizes the Kodak products mentioned in the video. How are changes in the company's product mix necessitating changes to the way managers market Kodak's offerings?
2. List the attributes of the Kodak brand. What benefits of branding has the company experienced over time? Have there been pitfalls to having a brand with such strong associations?
3. Describe the functions of packaging of a disposable camera.

Marketing & You Results

A higher score on this scale indicates that you are very brand conscious when you shop. You prefer to buy brands that are nationally known rather than private brands or generic brands. Conversely, a lower score suggests that you are not so brand conscious and tend to choose lower-priced, lesser-known brands.

ANATOMY OF A Packaging Decision

Barbie

Mattel updated Barbie's packaging to keep her fresh and familiar.

1 Familiar brand mark

2 Heat- and impact-tested packaging protects Barbie from damage.

3 Die cuts keep Barbie from shifting.

4 Plastic staples facilitate easy removal.

5 Persuasive labeling—'easy for me'—assures parents their kids can open it themselves.

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CHAPTER 11

Developing and Managing Products

Learning Outcomes

LO 1 Explain the importance of developing new products and describe the six categories of new products

LO 2 Explain the steps in the new-product development process

LO 3 Explain why some products succeed and others fail

LO 4 Discuss global issues in new-product development

LO 5 Explain the diffusion process through which new products are adopted

LO 6 Explain the concept of product life cycles

LO 1

The Importance of New Products

New products are important to sustain growth, increase revenues and profits, and replace obsolete items. The 25 most innovative companies in the world have achieved profit margin growth averaging 3.4 percent since 1995 compared to 0.4 percent for the average Standard and Poor's Global 1200 company.[1] Royal Philips Electronics, the $40 billion Dutch company that makes everything from televisions to MRI machines, reported that 49 percent of its 2005 revenues came from products introduced in the previous 12 months, up from 25 percent in 2003.[2] A study conducted by IBM revealed that nearly a third of consumer products companies had more than 20 percent of their annual sales generated by new products launched within the previous year.[3]

While nearly two-thirds of the senior managers included in a Boston Consulting Group survey reported that innovation was one of their top three priorities, nearly half said they were dissatisfied with their returns on investment in that area.[4] Apple Computer Corp. and Sony Corp. are both innovative companies that have experienced declining profits in recent times. Apple lost money in three of the past 10 years. However, Apple has experienced strong profits since the first iPod was introduced.[5]

Innovation is now a priority for many firms around the world, just as quality was in the 1980s, followed by cost cutting, just-in-time inventories, and outsourcing in the 1990s and early 2000s.[6] The term "innovation" is used in various contexts today. It describes new technologies, strategies, business models, business processes, and products. In this chapter we focus on new products, processes for developing new products, and how new products spread among consumers or business users, locally, nationally, and globally.

Being first on the market has a number of advantages. These include:[7]

- *Increased sales through longer sales life*: The earlier the product reaches the market, relative to the competition, the longer its life can be.
- *Increased margins*: The more innovative the product (i.e., the longer it remains unchallenged on the market), the longer consumers will accept a premium purchase price.
- *Increased product loyalty*: Early adopters are likely to upgrade, customize, or purchase companion products.
- *More resale opportunities*: For components, commodities, or products that other companies can private-label, being first to market can often help ensure sales in other channels.
- *Greater market responsiveness*: The faster companies can bring products to market that satisfy new or changing customer needs, the greater the opportunity to capitalize on those products for margin lift and to increase brand recognition.

Marketing & You

Using the following scale, indicate your opinion on the line before each item.

1	2	3	4	5	6
Strongly disagree					Strongly agree

— I like introducing my friends to new brands and products.

— I like helping people by providing them with information about various kinds of products.

— People ask me for information about products, places to shop, or sales.

— If someone asked where to get the best buy on several types of products, I could tell him or her where to shop.

— My friends think of me as a good source of information when it comes to new products or sales.

— I know a lot of different products, stores, and sales, and I like sharing this information.

Total your score. Read the chapter and find out what your score means at the end.

- *A sustained leadership position*: Being first is the market position a competitor cannot take away. And repeated firsts establish companies as innovators and leaders in the market.

CATEGORIES OF NEW PRODUCTS

The term new product is somewhat confusing because its meaning varies widely. Actually, the term has several "correct" definitions. A product can be new to the world, to the market, to the producer or seller, or to some combination of these. There are six categories of new products:

- *New-to-the-world products* (also called *discontinuous innovations*): These products create an entirely new market. New-to-the-world products represent the smallest category of new products. Ten of the most important new-to-the-world products introduced in the past 100 years are:[8]

    1. Penicillin
    2. Transistor radio
    3. Polio vaccine
    4. Mosaic (the first graphic Web browser)
    5. Microprocessor
    6. Black-and-white television
    7. Plain paper copier
    8. Alto personal computer (prototype of today's PCs)
    9. Microwave oven
    10. Arpanet network (the groundwork for the Internet)

PR NEWSFOTO/© LYSOL

New product lines are a type of new product that allows a company to enter an established market. With its Ready Brush toilet cleaning system, Lysol is entering the market for cleaning tools (toilet brushes, sponges, mops, etc.), which is dominated by companies like Ocello and Quickie.

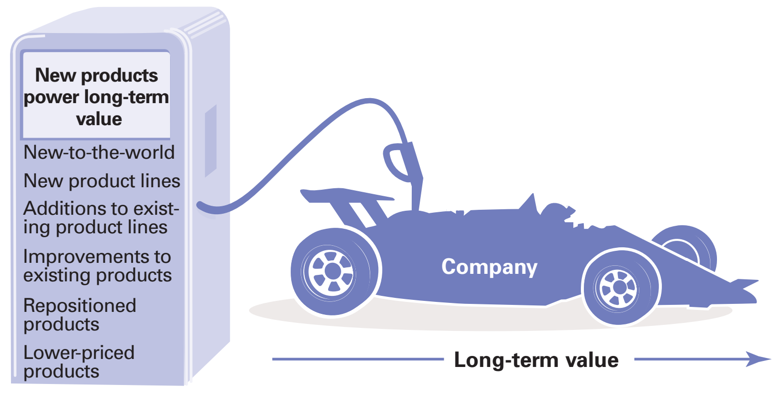
new product
A product new to the world, the market, the producer, the seller, or some combination of these.

- *New product lines*: These products, which the firm has not previously offered, allow it to enter new or established markets. For example, Disney Consumer Products recently added a new line of fragrances targeting 4–11 year old boys in Latin communities under the brand names Pirates of the Caribbean and Buzz Lightyear.[9]
- *Additions to existing product lines*: This category includes new products that supplement a firm's established line. For example, McDonald's Corp. recently introduced chicken snack wraps, which took only six months to become one of the most successful new product launches in McDonald's history.[10]
- *Improvements or revisions of existing products*: The "new and improved" product may be significantly or slightly changed. Kleenex Anti-Viral tissues, which include a new germ killing ingredient, and the Magic Eraser, which is Mr. Clean on a pretreated sponge, are examples of improved or revised products.[11]
- *Repositioned products*: These are existing products targeted at new markets or market segments, or repositioned to change the current market's perception of the product. Sometimes repositioning is intended to boost sales of a product with declining sales. Following a decline in sales, Diet Dr. Pepper was repositioned as an alternative to a dessert instead of a diet beverage.[12]
- *Lower-priced products*: This category refers to products that provide performance similar to competing brands at a lower price. Hewlett-Packard's Laser Jet 3100 is a scanner, copier, printer, and fax machine combined. This product

is priced lower than many conventional color copiers and much lower than the combined price of the four items purchased separately. Wal-Mart is making headway penetrating the low-price fashion market dominated by Target.

REVIEW LEARNING OUTCOME

LO 1 Explain the importance of developing new products and describe the six categories of new products



LO 2 The New-Product Development Process

Exhibit 11.1

New-Product Development Process

The management consulting firm Booz, Allen, & Hamilton has studied the new-product development process for over 30 years. After analyzing five major studies undertaken during this period, the firm concluded that the companies most likely to succeed in developing and introducing new products are those that take the following actions:

- Make the long-term commitment needed to support innovation and new-product development.
- Use a company-specific approach, driven by corporate objectives and strategies, with a well-defined new-product strategy at its core.
- Capitalize on experience to achieve and maintain competitive advantage.
- Establish an environment—a management style, organizational structure, and degree of top-management support—conducive to achieving company-specific new-product and corporate objectives.

Most companies follow a formal new-product development process, usually starting with a new-product strategy. Exhibit 11.1 traces the seven-step process, which is discussed in detail in this section. The exhibit is funnel-shaped to highlight the fact that each stage acts as a screen. The purpose is to filter out unworkable ideas.

NEW-PRODUCT STRATEGY

new-product strategy
A plan that links the new-product development process with the objectives of the marketing department, the business unit, and the corporation.

A new-product strategy links the new-product development process with the objectives of the marketing department, the business unit, and the corporation. A new-product strategy must be compatible with these objectives, and in turn, all three objectives must be consistent with one another. A new-product strategy is part of the organization's overall marketing strategy. It sharpens the focus and provides general guidelines for generating, screening, and evaluating new-product ideas. The new-product strategy specifies the roles that new products must play in the organization's overall plan and describes the characteristics of products the organization wants to offer and the markets it wants to serve.

The importance of a well-thought-out new-product strategy is illustrated by a Dun & Bradstreet finding that for each successful new product introduced, a company needs between 50 and 60 other new-product ideas somewhere in the new-product development process.[13] Gillette aims for 40 percent of annual sales to be generated from products less than five years old.[14]

Each year, *BusinessWeek* and the Boston Consulting Group identify the world's most innovative companies. In 2007, the top ten were:

- Apple
- Google
- Toyota
- General Electric
- Microsoft
- Procter & Gamble
- 3M
- Walt Disney
- IBM
- Sony

All but Walt Disney were among the top 13 in the *BusinessWeek*-Boston Consulting Group's 2006 list.[15]

IDEA GENERATION

New-product ideas come from many sources, including customers, employees, distributors, competitors, vendors, research and development (R&D), and consultants.

- *Customers*: The marketing concept suggests that customers' wants and needs should be the springboard for developing new products. Many of today's most innovative and successful marketers are introducing fewer new products, but they are taking steps to ensure that these "chosen few" are truly unique and better and, above all, really do address unmet consumer needs. How do they do that? They begin and end development with the customer. For example, Procter & Gamble uses surveys and personal observation to identify potential new products or uses. Researchers spend hours asking consumers questions and simply watching them go about household tasks. Mr. Clean's AutoDry product line and Magic Eraser, a wall spot cleaner, were inspired by observing customers performing routine tasks at home.[16] The key is to correctly identify customer needs and meet their requirements for product specifications.[17]
- *Employees*: Marketing personnel—advertising and marketing research employees, as well as salespeople—often create new-product ideas because they analyze

and are involved in the marketplace. The very successful introduction of Post-It Notes started with an employee's idea. In 1974, the R&D department of 3M's commercial tape division developed and patented the adhesive component of Post-It Notes. However, it was a year before an employee of the commercial tape division, who sang in a church choir, identified a use for the adhesive. He had been using paper clips and slips of paper to mark places in hymn books. But the paper clips damaged his books, and the slips of paper fell out. The solution, as we now all know, was to apply the adhesive to small pieces of paper and sell them in packages.

Some companies have developed innovation centers to encourage and implement new ideas. For example, McDonald's has a team of 70 employees who test new equipment ideas and procedures at its Innovation Center in Romeoville, Illinois.[18]

Some firms reward employees for coming up with creative new ideas. For example, Nokia Corp. recognizes employees with at least 10 patents in a formal awards ceremony. Each year, 3M provides 12–15 grants ranging from $50,000 to $100,000 to scientists who want to work on pet projects. Grant money can be used to hire staff or purchase equipment.[19]

- *Distributors:* A well-trained sales force routinely asks distributors about needs that are not being met. Because they are closer to end users, distributors are often more aware of customer needs than are manufacturers. The inspiration for Rubbermaid's litter-free lunch box, named Sidekick, came from a distributor, who suggested that Rubbermaid place some of its plastic containers inside a lunch box and sell it as an alternative to plastic wrap and paper bags.
- *Competitors*: No firms rely solely on internally generated ideas for new products. A big part of any organization's marketing intelligence system should be monitoring the performance of competitors' products. One purpose of competitive monitoring is to determine which, if any, of the competitors' products should be copied. There is plenty of information about competitors on the World Wide Web. For example, AltaVista (**http://www.altavista.digital.com**) is a powerful index tool that can be used to locate information about products and companies. Fuld & Co.'s competitive intelligence guide provides links to a variety of market intelligence sites.
- *Vendors*: 7-Eleven regularly forges partnerships with vendors to create proprietary products such as Candy Gulp (a plastic cup filled with gummies) and Blue Vanilla Laffy Taffy Rope candy (developed by Nestlè's Wonka division) exclusively for 7-Eleven.
- *Research and development*: R&D is carried out in four distinct ways. Basic research is scientific research aimed at discovering new technologies. Applied research takes these new technologies and tries to find useful applications for them. Product development goes one step further by converting applications into marketable products. *Product modification* makes cosmetic or functional changes in existing products. Many new-product breakthroughs come from R&D activities. Procter & Gamble Co., the world's largest household goods manufacturer, has 9,000 research and development employees.[20]

product development
A marketing strategy that entails the creation of marketable new products; the process of converting applications for new technologies into marketable products.

Some companies establish innovation laboratories to complement or even replace lengthy R&D programs in which scientists spend years coming up with new-product ideas and then pass these ideas along to product developers, then to designers, and finally to marketers.[21] Ideas labs focus on speeding innovation. Motorola's Razr telephone was developed in an innovation lab called Moto City, located about 50 miles from company headquarters. Most of the development work was done by a team of engineers, designers, and marketers who worked in open spaces and waist-high cubicles. Many normal practices, such as soliciting input

PR NEWSFOTO/© CINGULAR WIRELESS

from regional managers around the world, were omitted to foster teamwork and speed development.[22] A wide range of organizations including Boeing, Wrigley, Procter & Gamble, and the Mayo Clinic, use innovation labs.

- *Consultants*: Outside consultants are always available to examine a business and recommend product ideas. Examples include the Weston Group; Booz, Allen, & Hamilton; and Management Decisions. Traditionally, consultants determine whether a company has a balanced portfolio of products and, if not, what new-product ideas are needed to offset the imbalance. For instance, an outside consultant conceived Airwick's highly successful Carpet Fresh carpet cleaner.

Creativity is the wellspring of new-product ideas, regardless of who comes up with them. A variety of approaches and techniques have been developed to stimulate creative thinking. The two considered most useful for generating new-product ideas are brainstorming and focus-group exercises. The goal of brainstorming is to get a group to think of unlimited ways to vary a product or solve a problem. Group members avoid criticizing an idea, no matter how ridiculous it may seem. Objective evaluation is postponed. The sheer quantity of ideas is what matters. As noted in Chapter 9, an objective of focus-group interviews is to stimulate insightful comments through group interaction. Focus groups usually consist of seven to ten people. Sometimes consumer focus groups generate excellent new-product ideas—for example, Cycle dog food, Stick-Up room deodorizers, and Dustbuster vacuum cleaners. In the industrial market, machine tools, keyboard designs, aircraft interiors, and backhoe accessories have evolved from focus groups.

brainstorming
The process of getting a group to think of unlimited ways to vary a product or solve a problem.

screening
The first filter in the product development process, which eliminates ideas that are inconsistent with the organization's new-product strategy or are obviously inappropriate for some other reason.

concept test
A test to evaluate a new-product idea, usually before any prototype has been created.

business analysis
The second stage of the screening process where preliminary figures for demand, cost, sales, and profitability are calculated.

IDEA SCREENING

After new ideas have been generated, they pass through the first filter in the product development process. This stage, called screening, eliminates ideas that are inconsistent with the organization's new-product strategy or are obviously inappropriate for some other reason. The new-product committee, the new-product department, or some other formally appointed group performs the screening review. At General Motors, only one out of every 20 new car concepts developed will ever become a reality. That's not a bad percentage. In the pharmaceutical business, one new product out of 5,000 ideas is typical.[23] Most new-product ideas are rejected at the screening stage.

Concept tests are often used at the screening stage to rate concept (or product) alternatives. A concept test evaluates a new-product idea, usually before any prototype has been created. Typically, researchers get consumer reactions to descriptions and visual representations of a proposed product.

Concept tests are considered fairly good predictors of success for line extensions. They have also been relatively precise predictors of success for new products that are not copycat items, are not easily classified into existing product categories, and do not require major changes in consumer behavior—such as Betty Crocker Tuna Helper, Cycle dog food, and Libby Fruit Float. However, concept tests are usually inaccurate in predicting the success of new products that create new consumption patterns and require major changes in consumer behavior—such as microwave ovens, computers, and word processors.

BUSINESS ANALYSIS

New-product ideas that survive the initial screening process move to the business analysis stage, in which preliminary figures for demand, cost, sales, and profitability are calculated. For the first time, costs and revenues are estimated and compared.

Depending on the nature of the product and the company, this process may be simple or complex.

The newness of the product, the size of the market, and the nature of the competition all affect the accuracy of revenue projections. In an established market, like that for soft drinks, industry estimates of total market size are available. Forecasting market share for a new entry is a bigger challenge.

Xerox uses focus groups to assess the desirability of new copier features and to assess potential demand. This process played a key role in the design of the company's dual-engine Nuvera 288 Digital Perfecting System.[24]

Analyzing overall economic trends and their impact on estimated sales is especially important in product categories that are sensitive to fluctuations in the business cycle. If consumers view the economy as uncertain and risky, they will put off buying durable goods like major home appliances, automobiles, and homes. Likewise, business buyers postpone major equipment purchases if they expect a recession.

These questions are commonly asked during the business analysis stage:

- What is the likely demand for the product?
- What impact would the new product probably have on total sales, profits, market share, and return on investment?
- How would the introduction of the product affect existing products? Would the new product cannibalize existing products?
- Would current customers benefit from the product?
- Would the product enhance the image of the company's overall product mix?
- Would the new product affect current employees in any way? Would it lead to hiring more people or reducing the size of the workforce?
- What new facilities, if any, would be needed?
- How might competitors respond?
- What is the risk of failure? Is the company willing to take the risk?

Answering these questions may require studies of markets, competition, costs, and technical capabilities. But at the end of this stage, management should have a good understanding of the product's market potential. This understanding is important because costs increase dramatically once a product idea enters the development stage.

development
The stage in the product development process in which a prototype is developed and a marketing strategy is outlined.

New ideas often face resistance, especially if they are perceived as risky for the company. The ideas that survive the business analysis stage are often those whose creators blend a careful balance of political and managerial support early in the process.[25]

PR NEWSFOTO/© BOEING

Specially equipped Boeing 737 will enable commercial airlines to offer passengers real-time high-speed Internet and intranet access, television and full-featured e-mail capability.

DEVELOPMENT

In the early stage of development, the R&D or engineering department may develop a prototype of the product. During this stage, the firm should start sketching a marketing strategy. The marketing department should decide on the product's packaging, branding, labeling, and so forth. In addition, it should map out preliminary promotion, price, and distribution strategies. The feasibility of manufacturing the product at an acceptable cost should be thoroughly examined.

The development stage can last a long time and thus be very expensive. Crest toothpaste was in the development stage for 10 years. It took 18 years to develop Minute Rice, 15 years to develop the Polaroid Colorpack camera, 15 years to develop the Xerox copy machine, and 51 years to develop television. Gillette developed three shaving systems over a 27-year period (TracII, Atra, and Sensor) before introducing the Mach3 in 1998 and the Fusion in 2006.[26]

The development process works best when all the involved areas (R&D, marketing, engineering, production, and even suppliers) work together rather than sequentially, a process called simultaneous product development. This approach lets firms shorten the development process and reduces costs. With simultaneous product development, all relevant functional areas and outside suppliers participate in all stages of the development process. Rather than proceeding through highly structured stages, the cross-functional team operates in unison. Involving key suppliers early in the process capitalizes on their knowledge and enables them to develop critical component parts.

simultaneous product development
A team-oriented approach to new-product development.

test marketing
The limited introduction of a product and a marketing program to determine the reactions of potential customers in a market situation.

The Internet is a useful tool for implementing simultaneous product development. On the Net, multiple partners from a variety of locations can meet regularly to assess new-product ideas, analyze markets and demographics, and review cost information. Ideas judged to be feasible can quickly be converted into new products. Without the Internet, it would be impossible to conduct simultaneous product development from different parts of the world. Global R&D is important for two reasons. First, large companies have become global and no longer focus on one single market. Global R&D is necessary to connect with customers in different parts of the world. Second, companies want to tap into the world's best talent.

Some firms use online brain trusts to solve technical problems. InnoCentive, Inc., is a network of 80,000 self-selected science problem solvers in 173 countries. Its clients include Boeing, DuPont, and Procter & Gamble. Procter & Gamble has another program called the Connect-and-Develop Model. When the company selects an idea for development, it no longer tries to develop it from the ground up with its own resources and time. Instead, it issues a brief to its network of thinkers, researchers, technology entrepreneurs, and inventors around the world, hoping to generate dialog, suggestions, and solutions.[27]

Innovative firms also gather a variety of R&D input from customers online. Google polls millions of Web page creators to determine the most relevant search results. LEGO Group uses the Internet to identify its most enthusiastic customers and to help design and market products. Dow Chemical, Eli Lilly & Co., and Hewlett-Packard are among the firms that conduct online R&D activities.[28]

Laboratory tests are often conducted on prototype models during the development stage. User safety is an important aspect of laboratory testing, which actually subjects products to much more severe treatment than that anticipated by end users. The Consumer Product Safety Act of 1972 requires manufacturers to conduct a "reasonable testing program" to ensure that their products conform to established safety standards.

Many products that test well in the laboratory are also tried out in homes or businesses. Examples of product categories well suited for such use tests include human and pet food products, household cleaning products, and industrial chemicals and supplies. These products are all relatively inexpensive, and their performance characteristics are apparent to users. For example, Procter & Gamble tests a variety of personal and home-care products in the community around its Cincinnati, Ohio headquarters.

TEST MARKETING

After products and marketing programs have been developed, they are usually tested in the marketplace. Test marketing is the limited introduction of a product and a marketing program to determine the reactions of potential customers in a market situation. Test marketing allows management to evaluate alternative strategies and

Exhibit 11.2

Checklist for Selecting Test Markets

In choosing a test market, many criteria need to be considered, especially the following:

- Similarity to planned distribution outlets
- Relative isolation from other cities
- Availability of cooperative advertising media
- Diversified cross-section of ages, religions, cultural-societal preferences, etc.
- No atypical purchasing habits
- Representative population size
- Typical per capita income
- Good record as a test city, but not overly used
- Not easily "jammed" by competitors
- Stability of year-round sales
- No dominant television station; multiple newspapers, magazines, and radio stations
- Availability of research and audit services
- Availability of retailers that will cooperate
- Freedom from unusual influences, such as one industry's dominance or heavy tourism

assess how well the various aspects of the marketing mix fit together. Even established products are test marketed to assess new marketing strategies.

The cities chosen as test sites should reflect market conditions in the new product's projected market area. Yet no "magic city" exists that universally represents market conditions, and a product's success in one city doesn't guarantee that it will be a nationwide hit. When selecting test market cities, researchers should therefore find locations where the demographics and purchasing habits mirror the overall market. The company should also have good distribution in test cities. Moreover, test locations should be isolated from the media. If the TV stations in a particular market reach a very large area outside that market, the advertising used for the test product may pull in many consumers from outside the market. The product may then appear more successful than it really is. Exhibit 11.2 provides a useful checklist of criteria for selecting test markets.

The High Costs of Test Marketing

Test marketing frequently takes one year or longer, and costs can exceed $1 million. Some products remain in test markets even longer. McDonald's spent 12 years developing and testing salads before introducing them. Despite the cost, many firms believe it is better to fail in a test market than in a national introduction.

Because test marketing is so expensive, some companies do not test line extensions of well-known brands. For example, because the Folgers brand is well known, Procter & Gamble faced little risk in distributing its instant decaffeinated version nationally. Consolidated Foods Kitchen of Sara Lee followed the same approach with its frozen croissants. Other products introduced without being test marketed include General Foods' International Coffees, Quaker Oats' Chewy Granola Bars and Granola Dipps, and Pillsbury's Milk Break Bars.

The high cost of test marketing is not just financial. One unavoidable problem is that test marketing exposes the new product and its marketing mix to competitors before its introduction. Thus, the element of surprise is lost. Competitors can also sabotage or "jam" a testing program by introducing their own sales promotion, pricing, or advertising campaign to hide or distort the normal conditions that the testing firm might expect in the market.

Alternatives to Test Marketing

simulated (laboratory) market testing
The presentation of advertising and other promotion materials for several products, including a test product, to members of the product's target market.

Many firms are looking for cheaper, faster, and safer alternatives to traditional test marketing. In the early 1980s, Information Resources, Inc., pioneered one alternative: single-source research using supermarket scanner data (discussed in Chapter 9). A typical scanner test costs about $300,000. Another alternative to traditional test marketing is simulated (laboratory) market testing. Advertising and other promotional

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materials for several products, including the test product, are shown to members of the product's target market. These people are then taken to shop at a mock or real store, where their purchases are recorded. Shopper behavior, including repeat purchasing, is monitored to assess the product's likely performance under true market conditions. Research firms offer simulated market tests for $25,000 to $100,000, compared to $1 million or more for full-scale test marketing.

Online Test Marketing

Despite these alternatives, most firms still consider test marketing essential for most new products. The high price of failure simply prohibits the widespread introduction of most new products without testing. Many firms find that the Internet offers a fast, cost-effective way to conduct test marketing.

Procter & Gamble uses the Internet to assess customer demand for potential new products. Many products that are not available in grocery stores or drugstores can be sampled from P&G's corporate Web site (**http://www.pg.com**).

Other consumer goods firms that use online test marketing include General Mills and Quaker Oats. Other Web sites have appeared that offer consumers prototype products developed by all sizes of firms.

COMMERCIALIZATION

commercialization
The decision to market a product.

The final stage in the new-product development process is commercialization, the decision to market a product. The decision to commercialize the product sets several tasks in motion: ordering production materials and equipment, starting production, building inventories, shipping the product to field distribution points, training the sales force, announcing the new product to the trade, and advertising to potential customers.

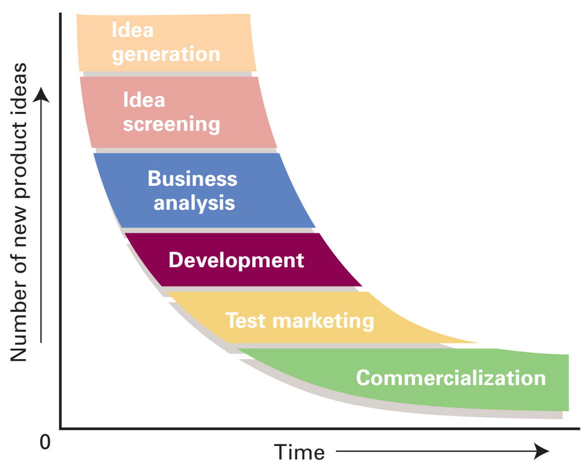
The time from the initial commercialization decision to the product's actual introduction varies. It can range from a few weeks for simple products that use existing equipment to several years for technical products requiring custom manufacturing equipment.

The total cost of development and initial introduction can be staggering. Gillette spent $750 million developing the Mach3, and its first-year marketing budget was $300 million.

For some products, a well-planned Internet campaign can provide new-product information for people who are looking for the solutions that a particular new product offers. Attempting to reach customers at the point in time when they need a product is much more cost-effective and efficient than communicating with a target market that may eventually need the product.

REVIEW LEARNING OUTCOME

LO 2 Explain the steps in the new-product development process



LO 3 Why Some Products Succeed and Others Fail

Despite the amount spent on developing and testing new products, a large proportion of new-product introductions fail. In the consumer goods industry, 70 to 90 percent of all new products fail within the first year.[29] Products fail for a number of reasons. Often they simply do not offer any discernible benefit compared to existing products. Another commonly cited factor in new-product failures is a poor match between product features and customer desires. For example, there are telephone systems on the market with over 700 different functions, but the average user is happy with just 10. Other reasons for failure include overestimation of market size, incorrect positioning, a price too high or too low, inadequate distribution, poor promotion, or simply an inferior product compared to those of competitors.

Interestingly, when managers are publicly committed to new products, they tend to stay committed even when new information indicates that the product will fail. This "escalation of commitment" can be disastrous for firms in today's hypercompetitive markets.[30]

Failure can be a matter of degree. Absolute failure occurs when a company cannot recoup its development, marketing, and production costs. The product actually loses money for the company. A relative product failure results when the product returns a profit but fails to achieve sales, profit, or market share goals. Some highly publicized new product failures include the Sony Betamax (1975), Apple Lisa (1983), New Coke (1985), and Kellogg's Breakfast Mates (1998).[31]

High costs and other risks of developing and testing new products do not stop many companies, such as Rubbermaid, Colgate-Palmolive, Campbell's Soup, 3M, and Procter & Gamble, from aggressively developing and introducing new products.

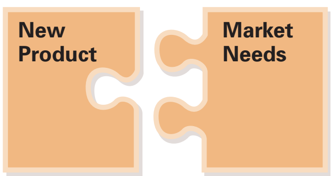
The most important factor in successful new-product introduction is a good match between the product and market needs—as the marketing concept would predict. Successful new products deliver a meaningful and perceivable benefit to a sizable number of people or organizations and are different in some meaningful way from their intended substitutes. Firms that routinely experience success in new-product introductions tend to share the following characteristics:[32]

- A history of carefully listening to customers
- An obsession with producing the best product possible
- A vision of what the market will be like in the future
- Strong leadership
- A commitment to new-product development
- A project-based team approach to new-product development
- Getting every aspect of the product development process right
- Willingness to fail occasionally

REVIEW LEARNING OUTCOME

LO3 Explain why some products succeed and others fail

Good match leads to success



Mismatch can mean failure

LO4
Global Issues in New-Product Development

Increasing globalization of markets and of competition provides a reason for multinational firms to consider new-product development from a worldwide perspective. That perspective includes developing countries as well as more established markets. As the Global Perspectives box in this chapter illustrates, many U.S. based firms are highly dependent on products developed specifically for unique needs in foreign markets.

A firm that starts with a global strategy is better able to develop products that are marketable worldwide. In many multinational corporations, every product is developed for potential worldwide distribution, and unique market requirements are built in whenever possible. Procter & Gamble introduced Pampers Phases into global markets within one month of introducing the product in the United States. P&G's goal was to have the product on shelves in 90 countries within one year. The objective was to establish brand loyalty among dealers and consumers before foreign competitors could react.

Some global marketers design their products to meet regulations in their major markets and then, if necessary, meet smaller markets' requirements country by country. Nissan develops lead-country car models that, with minor changes, can be sold in most markets. With this approach, Nissan has been able to reduce the number of its basic models from 48 to 18.

Developing countries represent huge automobile markets, but not at prevailing international prices. Renault SA introduced the Dacia Logan, an anonymous econocar with exposed screws, a coarse fabric interior, and a 90-horsepower motor. The Logan sells for about $7,300 in Eastern Europe and the Middle East, and $9,000 in Western Europe and has become more successful than predicted. Rivals such as Daimler Chrysler AG and Toyota Motor Corp. are preparing competitive entries priced under $10,000.[33]

Some companies could not sell their products at affordable prices and still make an adequate profit in many countries. To counter this problem, Procter & Gamble uses subcontractors to combine proprietary ingredients with standard chemicals and package the products.[34] The result is lower cost for P&G.

We often hear about how popular American products are in foreign countries. Recently, U.S. companies such as Levi Strauss, Coca-Cola, RJR Nabisco, and Nike have been finding that products popular in foreign markets can become hits in the United States. Haagen-Dazs's ice cream flavor *dulce de leche*, named after a caramelized milk drink that is popular in Argentina, was originally introduced in Buenos Aires. Enova, a cooking oil that helps cut body weight and fat, was the top-selling brand in Japan before it was introduced in the United States.

In other cases, former alliance partners have become competitors. For years, Shanghai Automotive Industry Corp. has worked with General Motors Corp. and Volkswagen AG to build cars for Chinese consumers. The Chinese auto maker now plans to introduce its own products in global markets, competing with its partners.[35]

GLOBAL Perspectives

Plastic Planet: For Tupperware, All the World's a Storage Container

Nearly 80 percent of Tupperware Brands' $1.3 billion revenue—and 95 percent of its profits—comes from outside North America. In most countries, Jel-Ring molds aren't what keep the home parties humming. Instead, Tupperware relies on local managers to inform designs—turning humdrum plastic into local solutions.

- **Bumbu Containers.**
  In Indonesia, Tupperware hired women execs who were attuned to local food practices. One result: a container for a mix of spices, called "*bumbu*," used to season meats. Bumbu, which includes star anise, cumin, and cardamom, is traditionally stored in tin containers that don't preserve flavors well. Tupperware seals in the aromatic spices—with a design considered fashionable enough to display on the dinner table.
- **Kimchi Keeper.**
  Kimchi, a spicy fermented-cabbage dish traditionally buried underground, is distinctively pungent. Tupperware's container features a tight but flexible seal to keep the stuff from flavoring other foods—while allowing gases produced by fermentation to escape. Tupperware CEO Rick Goings recalls being present when Korean workers simultaneously pulled the lids off their kimchi: "To be in a lunchroom in Korea—you just want to leave the room."
- **Cheesmart.**
  The French regard cheese as a living and changing food (unlike Americans, who just wrap it in plastic and stick it in the fridge). The company's researchers in Belgium labored to learn exactly how cheese goes bad. They developed a container with a semi-permeable membrane to reduce condensation, preventing mold. "There's a balance between keeping cheese soft and mold-free," says Goings. "If you seal it, you'll get green stuff."[36]

Make a list of other new uses for Tupperware containers.

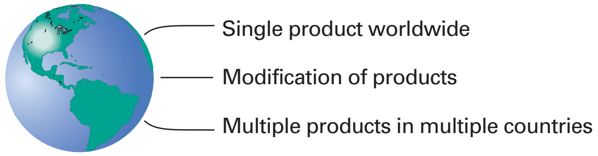
From Alyssa Danigelis, "Plastic Planet", 'Fast Company', September 2006, p. 39. Used with permission.

Global companies such as J&J have learned to capitalize on multinational talent. After it bought a small European brand called Compeed, it adapted the latter company's thick, cushiony bandages to create a waterproof Band-Aid that protects blisters.[37]

Other companies are applying a new twist to the popular international business aphorism, "think global, act local." At Coca-Cola, this means giving country managers more autonomy in new-product development. The idea has resulted in several new brands of energy drinks, waters, and teas introduced in various Asian countries. More beverages are planned to diversify beyond colas. Results have been impressive. The Global Perspectives box in this chapter provides other examples.

REVIEW LEARNING OUTCOME

LO4 Discuss global issues in new-product development



LO5 The Spread of New Products

adopter
A consumer who was happy enough with his or her trial experience with a product to use it again.

innovation
A product perceived as new by a potential adopter.

diffusion
The process by which the adoption of an innovation spreads.

Managers have a better chance of successfully marketing products if they understand how consumers learn about and adopt products. A person who buys a new product never before tried may ultimately become an adopter, a consumer who was happy enough with his or her trial experience with a product to use it again.

DIFFUSION OF INNOVATION

An innovation is a product perceived as new by a potential adopter. It really doesn't matter whether the product is "new to the world" or some other category of new product. If it is new to a potential adopter, it is an innovation in this context. Diffusion is the process by which the adoption of an innovation spreads.

Image not available due to copyright restrictions

Five categories of adopters participate in the diffusion process:

- *Innovators*: the first 2.5 percent of all those who adopt the product. Innovators are, almost obsessed, with trying new ideas and products, almost as an obsession. In addition to having higher incomes, they are more worldly and more active outside their community than noninnovators. They rely less on group norms and are more self-confident. Because they are well-educated, they are more likely to get their information from scientific sources and experts. Innovators are characterized as venturesome.
- *Early adopters*: the next 13.5 percent to adopt the product. Although early adopters are not the very first, they do adopt early in the product's life cycle. Compared to innovators, they rely much more on group norms and values. They are also more oriented to the local community, in contrast to the innovators' worldly outlook. Early adopters are more likely than innovators to be opinion leaders because of their closer affiliation with groups. Apple Computer spends its entire marketing budget attempting to appeal to early adopters. Joe Bates, research director for the Consumer Electronics Association, notes that early adopters spend up to three times more money on consumer electronics devices than other categories of adopters and are two- to

Exhibit 11.3

Who are early adopters?

- 77 million Americans, 36 million U.S. heads of household
- About 40 percent of Gen Xers (ages 28-41) are early adopters
- 49 percent own an MP3 player
- 70 percent have broadband Internet at home
- Roughly 60 percent are "sick of advertising today"
- 1.5 times more likely than the general population to own a laptop

SOURCE: Daniel B. Honigman, "Who's on First?" *Marketing News*, November 1, 2007, p. 15. Taken from Forrester Research's "The State of Consumers And Technology: Benchmark 2007" survey, September 2007. Used by permission of the American Marketing Association.

five-times more likely to spread the word about new products than average consumers.[38] The respect of others is a dominant characteristic of early adopters. Exhibit 11.3 identifies some other characteristics of early adopters.

- *Early majority:* the next 34 percent to adopt. The early majority weighs the pros and cons before adopting a new product. They are likely to collect more information and evaluate more brands than early adopters, therefore extending the adoption process. They rely on the group for information but are unlikely to be opinion leaders themselves. Instead, they tend to be opinion leaders' friends and neighbors. The early majority are an important link in the process of diffusing new ideas because they are positioned between earlier and later adopters. A dominant characteristic of the early majority is deliberateness.
- *Late majority*: the next 34 percent to adopt. The late majority adopts a new product because most of their friends have already adopted it. Because they also rely on group norms, their adoption stems from pressure to conform. This group tends to be older and below average in income and education. They depend mainly on word-of-mouth communication rather than on the mass media. The dominant characteristic of the late majority is skepticism.
- *Laggards*: the final 16 percent to adopt. Like innovators, laggards do not rely on group norms, but their independence is rooted in their ties to tradition. Thus, the past heavily influences their decisions. By the time laggards adopt an innovation, it has probably become outmoded and been replaced by something else. For example, they may have bought their first black-and-white TV set after color television was already widely diffused. Laggards have the longest adoption time and the lowest socioeconomic status. They tend to be suspicious of new products and alienated from a rapidly advancing society. The dominant value of laggards is tradition. Marketers typically ignore laggards, who do not seem to be motivated by advertising or personal selling and are virtually impossible to reach online. A study reported by the Pew Internet & American Life Project found that 18 percent of the U.S. population surveyed were "not interested in anything on the Internet" and another 8 percent were "not sure how to use the Internet."[39]

Note that some product categories, such as monochrome televisions, may never be adopted by 100 percent of the population. The adopter categories refer to all of those who will eventually adopt a product, not the entire population.

PRODUCT CHARACTERISTICS AND THE RATE OF ADOPTION

Five product characteristics can be used to predict and explain the rate of acceptance and diffusion of a new product:

- *Complexity*: the degree of difficulty involved in understanding and using a new product. The more complex the product, the slower is its diffusion. For instance, DVD recorders have been around for several years, but they were first purchased mostly by early adopters willing to go to the trouble of linking the gadgets to their PCs or to pay high prices for the first stand-alone machines that connect to a TV.

- *Compatibility*: the degree to which the new product is consistent with existing values and product knowledge, past experiences, and current needs. Incompatible products diffuse more slowly than compatible products. For example, the introduction of contraceptives is incompatible in countries where religious beliefs discourage birth control.
- *Relative advantage*: the degree to which a product is perceived as superior to existing substitutes. For example, because it reduces cooking time, the microwave oven has a clear relative advantage over a conventional oven.
- *Observability*: the degree to which the benefits or other results of using the product can be observed by others and communicated to target customers. For instance, fashion items and automobiles are highly visible and more observable than personal-care items.
- "*Trialability*": the degree to which a product can be tried on a limited basis. It is much easier to try a new toothpaste or breakfast cereal than a new automobile or microcomputer. Demonstrations in showrooms and test-drives are different from in-home trial use. To stimulate trials, marketers use free-sampling programs, tasting displays, and small package sizes.

Exhibit 11.4 shows the rate of adoption of five audio products introduced in the last 25 years. Satellite radio has been adopted more quickly than any other innovative audio product.

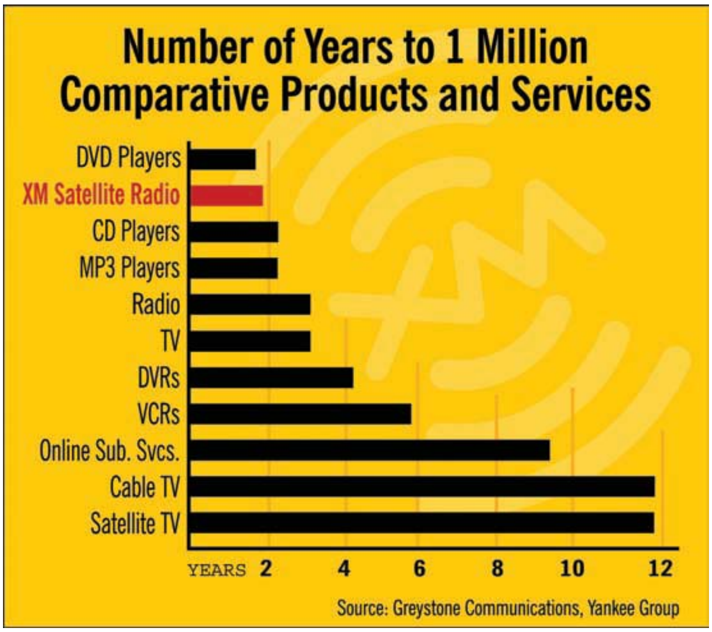
MARKETING IMPLICATIONS OF THE ADOPTION PROCESS

Two types of communication aid the diffusion process: *word-of-mouth communication* among consumers and communication from marketers to consumers. Word-of-mouth communication within and across groups speeds diffusion. Opinion leaders discuss new products with their followers and with other opinion leaders. Two recent studies found that consumers rated recommendations from others as the most important influence when purchasing a new product.[40] Marketers must therefore ensure that opinion leaders have the types of information desired in the media that they use. Suppliers of some products, such as professional and health-care services, rely almost solely on word-of-mouth communication for new business.

The Internet plays an important role in generating word-of-mouth communications. In fact, JWT Worldwide in New York estimates that over 85 percent of the country's top 1,000 marketing firms have some form of word-of-mouth communications strategy.[41] These efforts are often referred to as buzz marketing.

Often marketers recruit a core group of opinion leaders to get the buzz going. UPN recruited Alloy.com, a shopping and lifestyle site aimed at teenage girls, to develop a buzz campaign for the TV series America's Top Model. After analyzing

Exhibit 11.4
Sales of New Audio Products



© PR NEWSFOTO/© XMSATELLITE RADIO

the chatter on its site, Alloy identified 500 well-connected girls who had expressed interest in the show. Alloy provided the teens with America's Top Model party kits and encouraged them to invite an average of four friends over to their homes for gatherings themed around the TV show. According to Alloy, the results were very good.[42]

Business marketers have also developed strategies for obtaining online feedback and ideas from early adopters. Microsoft Corp. has a Most Valuable Professional (MVP) program with 4,000 participants in 90 countries. MVPs give Microsoft user feedback for almost every new product, from Windows to Xbox. Sony's Web community of about 850 early adopters is called "Sony Frontline."[43]

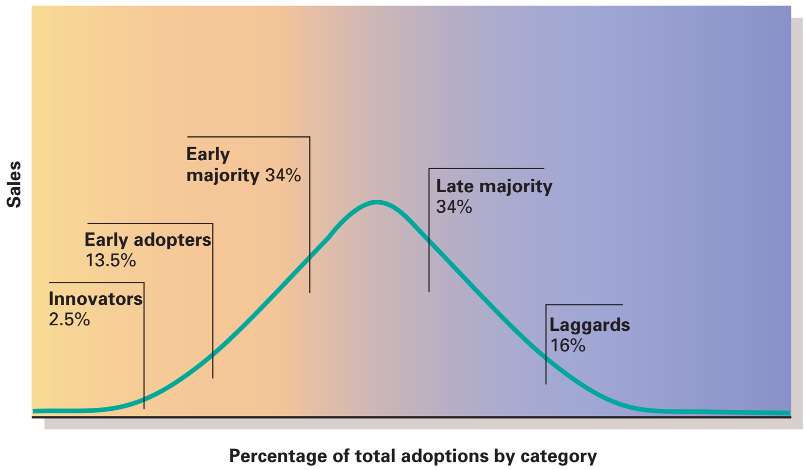
The second type of communication aiding the diffusion process is *communication directly from the marketer to potential adopters*. Messages directed toward early adopters should normally use different appeals than messages directed toward the early majority, the late majority, or the laggards. Early adopters are more important than innovators because they make up a larger group, are more socially active, and are usually opinion leaders.

Researchers at Doubleclick found that 39 percent of early adopters reported spending five or more hours online each day, compared to 23 percent of other categories of adopters. Furthermore, 40 percent of early adopters reported using Web sites to learn about products, compared to 31 percent of other categories of adopters. Also, 19 percent of early adopters reported using online advertising as an information source, compared to 8 percent of the other respondents.[44]

As the focus of a promotional campaign shifts from early adopters to the early majority and the late majority, marketers should study the dominant characteristics, buying behavior, and media characteristics of these target markets. Then they should revise messages and media strategy to fit. The diffusion model helps guide marketers in developing and implementing promotion strategy.

REVIEW LEARNING OUTCOME

LO 5 Explain the diffusion process through which new products are adopted



Product Characteristics (Influence Rate of Adoption)

- Complexity
- Compatibility
- Relative Advantage
- Observability
- "Trialability"

LO 6

Product Life Cycles

product life cycle (PLC) A biological metaphor that traces the stages of a product's acceptance, from its introduction (birth) to its decline (death).

The **product life cycle (PLC)** is one of the most familiar concepts in marketing. Although some researchers and consultants have challenged the theoretical basis and managerial value of the PLC, many believe it is a useful marketing management diagnostic tool and a general guide for marketing planning in various "life-cycle" stages.

The product life cycle is a biological metaphor that traces the stages of a product's acceptance, from its introduction (birth) to its decline (death). As Exhibit 11.5 shows, a product progresses through four major stages: introduction, growth, maturity, and decline.

Exhibit 11.5

Four Stages of the Product Life Cycle

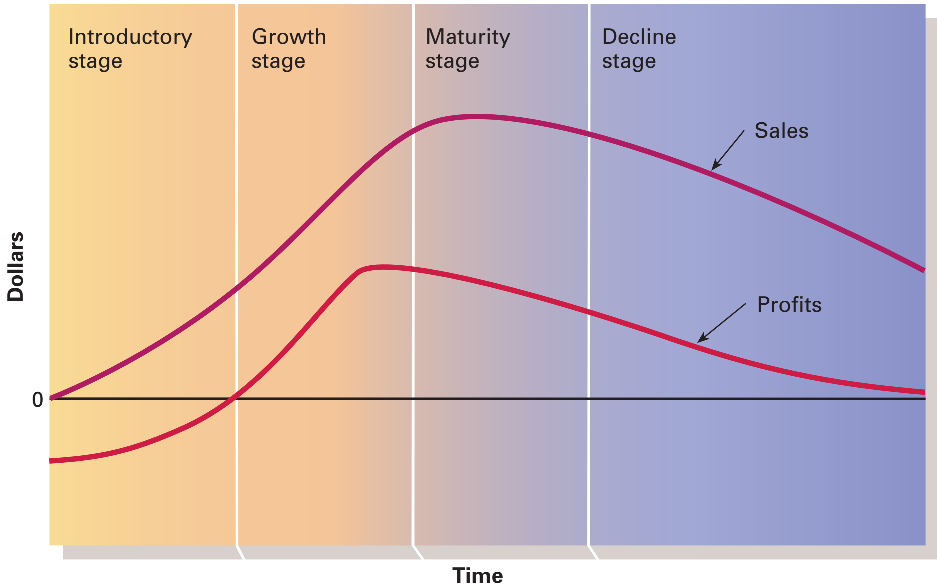
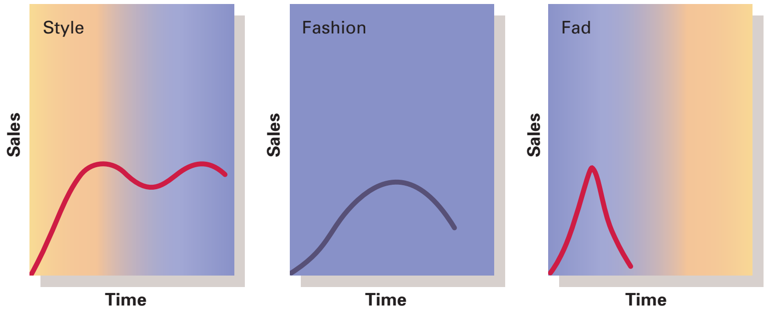


Exhibit 11.6

Product Life Cycles for Styles, Fashions, and Fads



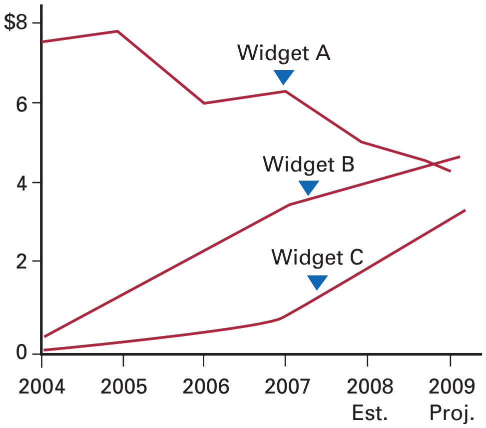
product category
All brands that satisfy a particular type of need.

The PLC concept can be used to analyze a brand, a product form, or a product category. The PLC for a product form is usually longer than the PLC for any one brand. The exception would be a brand that was the first and last competitor in a product form market. In that situation, the brand and product form life cycles would be equal in length. Product categories have the longest life cycles. A product category includes all brands that satisfy a particular type of need such as shaving products, passenger automobiles, or soft drinks.

The time a product spends in any one stage of the life cycle may vary dramatically. Some products, such as fad items, move through the entire cycle in weeks. Others, such as electric clothes washers and dryers, stay in the maturity stage for decades. Exhibit 11.5 illustrates the typical life cycle for a consumer durable good, such as a washer or dryer. In contrast, Exhibit 11.6 illustrates typical life cycles for styles (such as formal, business, or casual clothing), fashions (such as miniskirts or baggy jeans), and fads (such as leopard-print clothing). Changes in a product, its uses, its image, or its positioning can extend that product's life cycle.

Exhibit 11.7

U.S. Sales of "Widgets," in Billions of Dollars



As product life cycles continue to decrease, compressing development cycles and accelerating new product developments are critical.[45] The PLC concept does not tell managers the length of a product's life cycle or its duration in any stage. It does not dictate marketing strategy. It is simply a tool to help marketers forecast future events and suggest appropriate strategies. What conclusions can you draw about the PLC of the fictitious "Widget A," "Widget B," and "Widget C" in Exhibit 11.7 based on four and a half years of sales data?

INTRODUCTORY STAGE

introductory stage
The first stage of the product life cycle in which the full-scale launch of a new product into the marketplace occurs.

growth stage
The second stage of the product life cycle when sales typically grow at an increasing rate, many competitors enter the market, large companies may start acquiring small pioneering firms, and profits are healthy.

maturity stage
The third stage of the product life cycle during which sales increase at a decreasing rate.

The introductory stage of the product life cycle represents the full-scale launch of a new product into the marketplace. Computer databases for personal use, room-deodorizing air-conditioning filters, and wind-powered home electric generators are all product categories that have recently entered the PLC. A high failure rate, little competition, frequent product modification, and limited distribution typify the introductory stage of the PLC.

Marketing costs in the introductory stage are normally high for several reasons. High dealer margins are often needed to obtain adequate distribution, and incentives are needed to get consumers to try the new product. Advertising expenses are high because of the need to educate consumers about the new product's benefits. Production costs are also often high in this stage, as product and manufacturing flaws are identified and corrected and efforts are undertaken to develop mass-production economies.

As Exhibit 11.5 illustrates, sales normally increase slowly during the introductory stage. Moreover, profits are usually negative because of R&D costs, factory tooling, and high introduction costs. The length of the introductory phase is largely determined by product characteristics, such as the product's advantages over substitute products, the educational effort required to make the product known, and management's commitment of resources to the new item. A short introductory period is usually preferred in order to reduce the impact of negative earnings and cash flows. As soon as the product gets off the ground, the financial burden should begin to diminish. Also, a short introduction helps dispel some of the uncertainty as to whether the new product will be successful.

Promotion strategy in the introductory stage focuses on developing product awareness and informing consumers about the product category's potential benefits. At this stage, the communication challenge is to stimulate primary demand—demand for the product in general rather than for a specific brand. Intensive personal selling is often required to gain acceptance for the product among wholesalers and retailers. Promotion of convenience products often requires heavy consumer sampling and couponing. Shopping and specialty products demand educational advertising and personal selling to the final consumer.

GROWTH STAGE

If a product category survives the introductory stage, it advances to the growth stage of the life cycle. In this stage, sales typically grow at an increasing rate, many competitors enter the market, and large companies may start to acquire small pioneering firms. Profits rise rapidly in the growth stage, reach their peak, and begin declining as competition intensifies. Emphasis switches from primary demand promotion (for example, promoting personal digital assistants, or PDAs) to aggressive brand advertising and communication of the differences between brands (for example, promoting Casio versus Palm and Visor).

Distribution becomes a major key to success during the growth stage, as well as in later stages. Manufacturers scramble to sign up dealers and distributors and to build long-term relationships. Without adequate distribution, it is impossible to establish a strong market position.

MATURITY STAGE

A period during which sales increase at a decreasing rate signals the beginning of the maturity stage of the life cycle. New users cannot be added indefinitely, and sooner or later the market approaches saturation. Normally, this is the longest stage of the product life cycle. Many major household appliances are in the maturity stage of their life cycles.

For shopping products and many specialty products, annual models begin to appear during the maturity stage. Product lines are lengthened to appeal to additional market segments. Service and repair assume more important roles as manufacturers strive to distinguish their products from others. Product design changes tend to become stylistic (How can the product be made different?) rather than functional (How can the product be made better?).

As prices and profits continue to fall, marginal competitors start dropping out of the market. Dealer margins also shrink, resulting in less shelf space for mature items, lower dealer inventories, and a general reluctance to promote the product. Thus, promotion to dealers often intensifies during this stage in order to retain loyalty.

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Heavy consumer promotion by the manufacturer is also required to maintain market share. Consider these well-known examples of competition in the maturity stage: the "cola war" featuring Coke and Pepsi, the "beer war" featuring Anheuser-Busch's Budweiser brands and Philip Morris's Miller brands, and the "burger wars" pitting leader McDonald's against challengers Burger King and Wendy's.

Another characteristic of the maturity stage is the emergence of "niche marketers" that target narrow, well-defined, underserved segments of a market. Starbucks Coffee targets its gourmet line at the only segment of the coffee market that is growing: new, younger, more affluent coffee drinkers.

DECLINE STAGE

decline stage
The fourth stage of the product life cycle, characterized by a long-run drop in sales.

A long-run drop in sales signals the beginning of the decline stage. The rate of decline is governed by how rapidly consumer tastes change or substitute products are adopted. Many convenience products and fad items lose their market overnight, leaving large inventories of unsold items, such as designer jeans. Others die more slowly.

U.S. sales of traditional 35mm cameras have been on a steady decline since 2000. In one recent year, film camera sales dropped 15 percent. The worldwide shift to digital photography led Eastman Kodak to stop selling reloadable film-based consumer cameras in the United States, Canada, and Europe. Kodak hadn't made a profit selling film cameras for several years. It continued selling the cameras only to aid the sale of film. Kodak's first consumer camera was introduced in 1888.[46]

Some firms have developed successful strategies for marketing products in the decline stage of the product life cycle. They eliminate all nonessential marketing expenses and let sales decline as more and more customers discontinue purchasing the products. Eventually, the product is withdrawn from the market.

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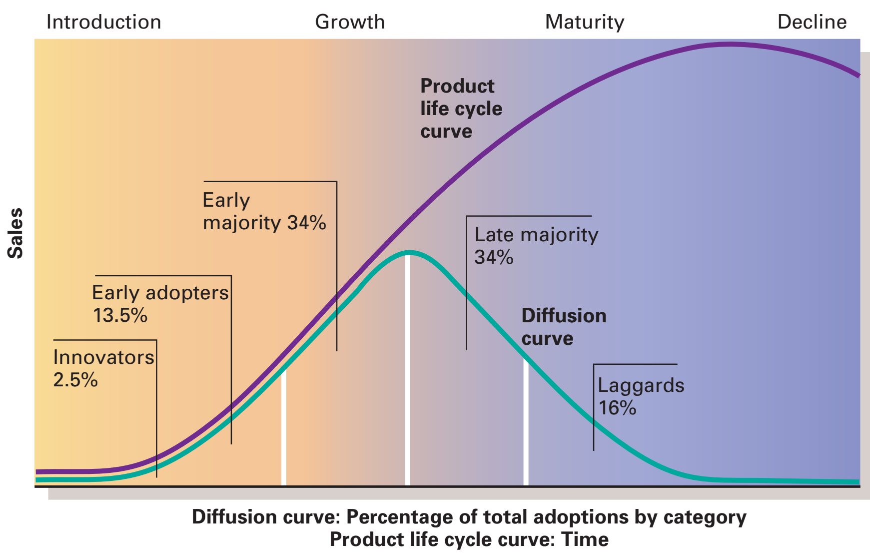
Management sage Peter Drucker says that all companies should practice "organized abandonment," which entails reviewing every product, service, and policy every two or three years and asking the critical question, "If we didn't do this already, knowing what we now do, would we go and do it?" In

Exhibit 11.8
Relationship between the Diffusion Process and the Product Life Cycle



other words, would the company introduce the product, service, or policy now? According to Drucker, if the answer is no, it's time to begin the abandonment process.[47]

IMPLICATIONS FOR MARKETING MANAGEMENT

The product life cycle concept encourages marketing managers to plan so that they can take the initiative instead of reacting to past events. The PLC is especially useful as a predicting or forecasting tool. Because products pass through distinctive stages, it is often possible to estimate a product's location on the curve using historical data. Profits, like sales, tend to follow a predictable path over a product's life cycle.

Exhibit 11.8 shows the relationship between the adopter categories and stages of the PLC. Note that the various categories of adopters first buy products in different stages of the life cycle. Almost all sales in the maturity and decline stages represent repeat purchasing.

REVIEW LEARNING OUTCOME

LO6 Explain the concept of product life cycles

Marketing Mix Strategy	Product Life Cycle Stage: Introductory	Growth	Maturity	Decline
Product Strategy	Limited number of models; frequent product modifications	Expanded number of models; frequent product modifications	Large number of models	Elimination of unprofitable models and brands
Distribution Strategy	Distribution usually limited, depending on product; intensive efforts and high margins often needed to attract wholesalers and retailers	Expanded number of dealers; intensive efforts to establish long-term relationships with wholesalers and retailers	Extensive number of dealers; margins declining; intensive efforts to retain distributors and shelf space	Unprofitable outlets phased out
Promotion Strategy	Develop product awareness; stimulate primary demand; use intensive personal selling to distributors; use sampling and couponing for consumers	Stimulate selective demand; advertise brand aggressively	Stimulate selective demand; advertise brand aggressively; promote heavily to retain dealers and customers	Phase out all promotion
Pricing Strategy	Prices are usually high to recover development costs (see Chapter 19)	Prices begin to fall toward end of growth stage as result of competitive pressure	Prices continue to fall	Prices stabilize at relatively low level; small price rises are possible if competition is negligible

Sales

Time

70 < employees testing ideas at McDonald's Innovation center

research and development employees at Procter & Gamble > **9,000**

18 < years spent developing Minute Rice

self-selected science problem solvers using the InnoCentive Inc. online brain trust > **80,000**

$1 million < cost of full-scale test marketing

amount Gillette spent to develop the Mach3 > **$750 million**

percentage of the U.S. population claiming they are "not sure how to use the Internet" > **8**

500 < girls recruited by Alloy.com to generate buzz about the TV show, America's Top Model

percent drop in film camera sales in recent years > **15**

850 < early adopters in the Sony Frontline Web community

Review and Applications

LO 1 Explain the importance of developing new products and describe the six categories of new products. New products are important to sustain growth and profits and to replace obsolete items. New products can be classified as new-to-the-world products (discontinuous innovations), new product lines, additions to existing product lines, improvements or revisions of existing products, repositioned products, or lower-priced products. To sustain or increase profits, a firm must innovate.

1.1 How many new products can you identify? Visit the supermarket and make a list of at least 15 items with the word "New" on the label. Include on your list anything that looks like a new product. Next to each item on your list, write the category of new product that best describes the item. Share your results with the class.

TEAM

1.2 New entertainment products aren't necessarily media products. Form a team of three or four students and brainstorm new nonmedia entertainment products. Try to identify one item for each of the categories of new products discussed in the chapter.

LO 2 Explain the steps in the new-product development process. First, a firm forms a new-product strategy by outlining the characteristics and roles of future products. Then new-product ideas are generated by customers, employees, distributors, competitors, vendors, and internal R&D personnel. Once a product idea has survived initial screening by an appointed screening group, it undergoes business analysis to determine its potential profitability. If a product concept seems viable, it progresses into the development phase, in which the technical and economic feasibility of the manufacturing process is evaluated. The development phase also includes laboratory and use testing of a product for performance and safety. Following initial testing and refinement, most products are introduced in a test market to evaluate consumer response and marketing strategies. Finally, test market successes are propelled into full commercialization. The commercialization process involves starting up production, building inventories, shipping to distributors, training a sales force, announcing the product to the trade, and advertising to consumers.

2.1 List the advantages of simultaneous product development.

WRITING

2.2 You are a marketing manager for Nike. Your department has come up with the idea of manufacturing a baseball bat for use in colleges around the nation. Assuming you are in the business analysis stage, write a brief analysis based on the questions in the "Business Analysis" section of the chapter.

2.3 What are the major disadvantages to test marketing, and how might they be avoided?

ONLINE

2.4 How could information from customer orders at **http://www.pizzahut.com** help the company's marketers plan new-product developments?

LO 3 Explain why some products succeed and others fail. The most important factor in determining the success of a new product is the extent to which the product matches the needs of the market. Good matches are frequently successful. Poor matches are not.

TEAM

3.1 In small groups, brainstorm ideas for a new wet-weather clothing line. What type of product would potential customers want and need? Prepare and deliver a brief presentation to your class.

LO 4 Discuss global issues in new-product development. A marketer with global vision seeks to develop products that can easily be adapted to suit local needs. The goal is not simply to develop a standard product that can be sold worldwide. Smart global marketers also look for good product ideas worldwide.

ONLINE

4.1 Visit **http://pg.com** and look at the brands it offers around the world. What conclusions can you draw about Procter & Gamble's global new-product development strategy?

LO 5 Explain the diffusion process through which new products are adopted. The diffusion process is the spread of a new product from its producer to ultimate adopters. Adopters in the diffusion process belong to five categories: innovators, early adopters, the early majority, the late majority, and laggards. Product characteristics that affect the rate of adoption include product complexity, compatibility with existing social values, relative advantage over existing substitutes, observability, and "trialability." The diffusion process is facilitated by word-of-mouth communication and communication from marketers to consumers.

5.1 Describe some products whose adoption rates have been affected by complexity, compatibility, relative advantage, observability, and/or "trialability."

5.2 What type of adopter behavior do you typically follow? Explain.

WRITING

5.3 Review Exhibit 11.4. Analyze each product on the graph according to the characteristics that influence the rate of adoption. For example, what can you conclude from the data about the relative advantage of DVD audio? Write one to two pages explaining your analysis.

LO6

Explain the concept of product life cycles. All brands and product categories undergo a life cycle with four stages: introduction, growth, maturity, and decline. The rate at which products move through these stages varies dramatically. Marketing managers use the product life cycle concept as an analytical tool to forecast a product's future and devise effective marketing strategies.

ONLINE

6.1 What is Cheerios doing to compete successfully in the maturity stage? Go to its Web site **http://www.cheerios.com** to find out.

Key Terms

adopter	336	growth stage	341	product life cycle (PLC)	339
brainstorming	329	innovation	336	screening	329
business analysis	329	introductory stage	341	simulated (laboratory) market testing	332
commercialization	333	maturity stage	341	simultaneous product development	331
concept test	329	new product	325	test marketing	331
decline stage	342	new-product strategy	327		
development	330	product category	340		
diffusion	336	product development	328		

Exercises

APPLICATION EXERCISE

A simple statistical analysis will help you better understand the types of new products. As in the Application Exercise in Chapter 6, you will be using print advertisements, but you will also be adding information from other sources (TV ads, trips to the store, and the like).[48]

Activities

1. Compile a list of 100 new products. If you are building a portfolio of ads (see the Application Exercise in Chapter 6), you can generate part of this list as you collect print advertisements for the topics in this chapter. Consider tabulating television ads for new products that are aired during programs you normally watch. A trip to the grocery could probably yield your entire list, but then it would be limited to consumer products.
2. Make a table with six columns labeled as follows: new-to-the-world products, new product line, addition to existing product line, improvement/revision of existing product line, repositioned product, and lower-priced product.
3. Place each of your 100 new products into one of the six categories. Tabulate your results at the bottom of each column. What conclusions can you draw from the distribution of your products? Consider adding your results together with the rest of the class to get a larger and more random sample.

ETHICS

ETHICS EXERCISE

One source of new-product ideas is competitors. Steven Fischer recently joined Frankie and Alex Specialty Products as a brand manager. His new boss told him, "We don't have a budget for new-product development. We just monitor our competitors' new-product introductions and offer knockoffs of any that look like they will be successful."

Questions

1. Is this practice ethical?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketingpower.com** and review the statement. Then, write a brief paragraph on what the AMA Statement of Ethics contains that relates to knockoff products.

Case Study: Kandy Kastle

WELCOME TO THE KANDY KASTLE, BUT BEWARE— THINGS ARE NOT WHAT THEY SEEM

Meet Larry Jones, a former toy designer for the likes of Hasbro, Mattel and Playmates Toys. Displaced when the industry turned to electronic toys, the irrepressible Jones is hard at play designing captivating candy concepts for niche manufacturer Kandy Kastle. He is not a confectioner, nor does he aspire to be one. Instead, Jones tinkers with candy delivery mechanisms and silly, sometimes grotesque names sure to capture the eyes, imaginations, and tastebuds of youngsters.

His products belong to the $250 million, nonchocolate segment of the U.S. novelty candy market. It's the third largest segment of the sweets market, behind chocolate and chewy treats such as gummy candies, licorice, and taffy. The market has been flat in recent years, but several former toy designers and a slew of hobbyist designers are beginning to breathe new life into the industry.

Their creations range from the simply fun to the outright goofy, and candy makers pay handsomely in hopes of landing the next big hit. Two of Jones's latest hits include the Big Barf and the Big Burp. Repulsive though they sound, both are just mouth-shaped, sound-generating dispensers for harmless gumballs. Though items like the Big Barf reek of a style unique to Larry Jones, he is just one of a new breed of novelty candy container designers who are hoping to create the next confection legend that might someday be mentioned in the same breath as the almighty Pez.

As action figures, toy trains, and other traditional toys are increasingly overshadowed by their digital counterparts, inventors and their employers are betting that products that combine toys with candy curiosities are positioned to capture the dollars left behind by that fading market. Deirdre Gonzalez, vice president of marketing for Cap Candy, says the reinvigorated novelty candy market is "a hybrid business between the two industries." Often priced from $.99 to $1.29, candy items sold with toy novelties are now attracting dollars that used to be reserved for low-end toy purchases.

And the competition is as fierce as children's tastes are fickle. In addition to Kandy Kastle, companies like Cap Candy and Candy Planet race each other to develop new products, while the likes of Willy Wonka and Jelly Belly battle to promote their lines with tie-ins to blockbuster children's movies. Even independent entrepreneurs are getting in on the act. Two married couples quit their postal service jobs to form BAAT Enterprises (from their names: Bill, Ann, Ann, and Tom) and introduced the Spin Pop, a rotating motorized sucker. A modern take on the Ring Pop, the Spin Pop sold almost 6 million units in under two years.

What's cool with kids is fleeting, though. New products must be developed every month to keep up. Larry Jones, for example, did not rest on the laurels of his gastrointestinal gumball designs. He is also the wiz behind Ear Wax, Big Toe Goo, Tar Pits, Hose Nose, Brain Drain, and glow-in-the-dark Lightning Bugs. "What I'm after is to have the kid have a little bit of magic or a little giggle while eating his candy," Jones says. Kandy Kastle is relying on him to come up with a host of interesting fare based on the hugely popular Hello Kitty brand, too. Originality is key. The children in this market space, aged 4 to 12 years, are increasingly savvy consumers and they are gaining influence and even buying power.

Influence with parents is crucial, of course, but sway with other kids in the peer group is more critical. Rose Downey, marketing manager at Au'Some Candy Company, puts extra emphasis on word-of-mouth endorsements for her company's novelty products. "We feel that the right way to grasp the kids' attention is word-of-mouth advertising," she says. "Kids trust other kids' judgment," she continues. "If Child A buys the product and it tastes great and looks cool and is fun, Child B is going to want the product and so on. Trust the kids. They know best when it comes to candy."[49]

Questions

1. To what category of new products does the Spin Pop belong?
2. Based on what you read in the case, what do you think Kandy Kastle's new-product development strategy is? Why do you think the development of the Hello Kitty product line is important?

3. Visit **http://www.KandyKastle.com** and review the product descriptions. Discuss the characteristics that influence their rate of adoption, and predict and explain their rates of acceptance and diffusion.
4. In what part of the product life cycle are the candy and toy categories? What kind of future do you predict for the novelty candy category?

Company Clips

KODAK—REINVENTING PHOTOGRAPHY

Designing usable and intriguing products is an integral part of Kodak's marketing process. Paul Porter, director of corporate design and usability, focuses on creating interesting, functional, and intuitive equipment. To make sure the company is on the right track with product development, Kodak marketers interview customers and visit them in their own homes, observing how families use digital photography. The understanding gained from these interactions helps the company create a wide range of products targeted at different market segments.

Questions

1. EasyShare 1 didn't sell very well, but Paul Porter claimed this wasn't the purpose of that particular product. What was the purpose of the product?
2. What kind of new product was EasyShare 1?
3. Discuss the product development process at Kodak.
4. Place Kodak's digital cameras in the product life cycle.

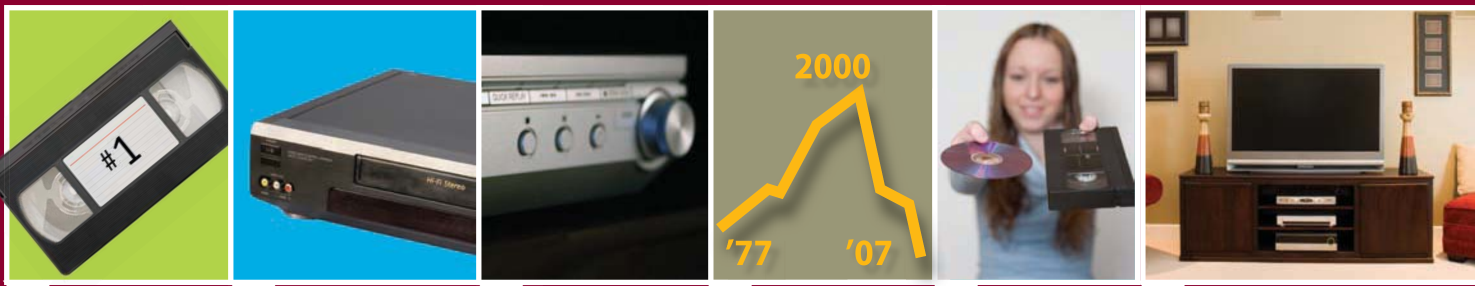
Marketing & You Results

If your score is high, you are most likely a "market maven." You are aware of new products earlier and talk about a variety of products to your friends. High scores also indicate a greater interest in and attentiveness to the market. Conversely, the lower your score, the less interested you are in the market and new products.

ANATOMY OF A Product Life Cycle

VCR

VCR sales dropped rapidly in the face of growing DVD competition.



1977
VHS first sold in the U.S.

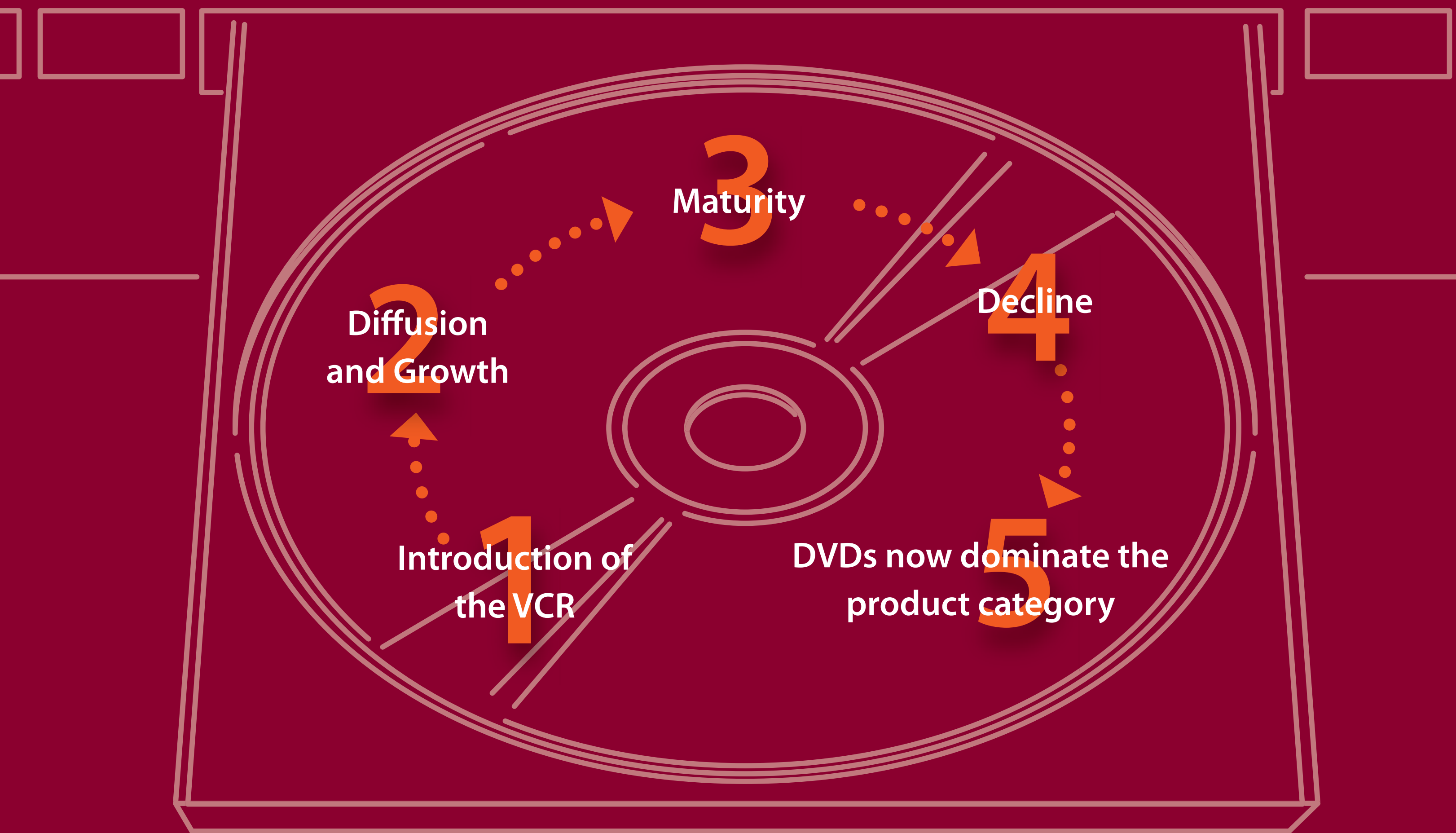
1992
100 millionth VCR sold

1997
First DVD titles released in the U.S.

2000
VCR sales peak at 23 million units

2001
DVD dollar sales surpass VHS sales

2006
More households own DVD players than VCRs



Services and Nonprofit Organization Marketing

CHAPTER 12

Learning Outcomes

- LO 1 Discuss the importance of services to the economy
- LO 2 Discuss the differences between services and goods
- LO 3 Describe the components of service quality and the gap model of service quality
- LO 4 Develop marketing mixes for services
- LO 5 Discuss relationship marketing in services
- LO 6 Explain internal marketing in services
- LO 7 Discuss global issues in services marketing
- LO 8 Describe nonprofit organization marketing

LO 1
The Importance of Services

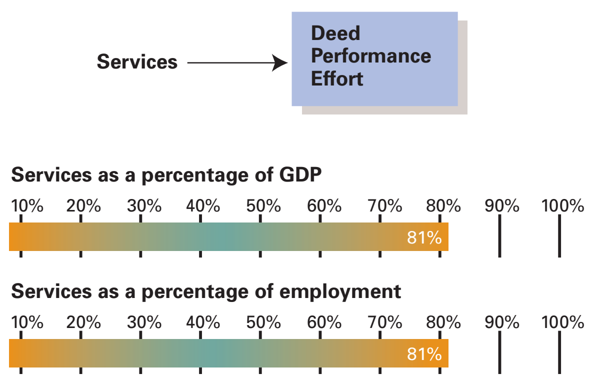
service
The result of applying human or mechanical efforts to people or objects.

A service is the result of applying human or mechanical efforts to people or objects. Services involve a deed, a performance, or an effort that cannot be physically possessed. Today, the service sector substantially influences the U.S. economy, accounting for 81 percent of both U.S. gross domestic product and U.S. employment.[1] The demand for services is expected to continue. According to the Bureau of Labor Statistics, service occupations will be responsible for nearly all net job growth through the year 2012. Much of this demand results from demographics. An aging population will need nurses, home health care, physical therapists, and social workers. Two-earner families need child-care, housecleaning, and lawn-care services. Also increasing will be the demand for information managers, such as computer engineers and systems analysts. There is also a growing market for service companies worldwide.

The marketing process described in Chapter 1 is the same for all types of products, whether they are goods or services. Many ideas and strategies discussed throughout this book have been illustrated with service examples. In many ways, marketing is marketing, regardless of the product's characteristics. In addition, although a comparison of goods and services marketing can be beneficial, in reality it is hard to distinguish clearly between manufacturing and service firms. Indeed, many manufacturing firms can point to service as a major factor in their success. For example, maintenance and repair services offered by the manufacturer are important to buyers of copy machines. General Electric makes most of its revenues from finance operations rather than from products. Nevertheless, services have some unique characteristics that distinguish them from goods, and marketing strategies need to be adjusted for these characteristics.

REVIEW LEARNING OUTCOME

LO 1 Discuss the importance of services to the economy



Marketing & You

What do you think about charities?

Using the following scale, enter your answers on the lines provided

1 - Strongly agree
2 - Moderately agree
3 - Agree
4 - Moderately disagree
5 - Strongly disagree

— The money given to charities goes for good causes.

— Much of the money donated to charity is wasted.*

— My image of charitable organizations is positive.

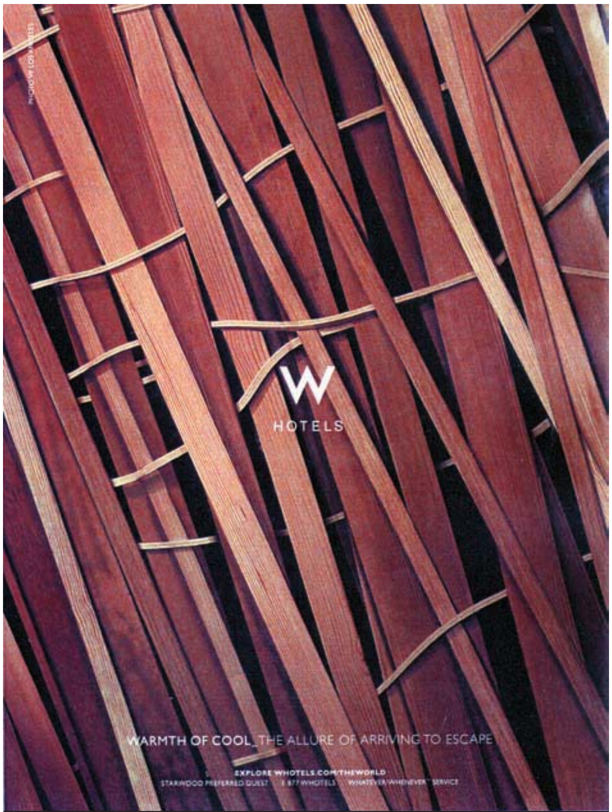
— Charitable organizations have been quite successful in helping the needy.

— Charity organizations perform a useful function for society.

Total your score, reversing your answer for the item followed by an asterisk. That is, if you answered 2, change it to 4, and vice versa. Read the chapter, and find out what your score means at the end.

LO 2
How Services Differ from Goods

Services have four unique characteristics that distinguish them from goods. Services are intangible, inseparable, heterogeneous, and perishable.



Hotels offer an intangible service rather than a solid product. This advertisement for W Hotels uses the simple image of woven rush to convey luxury and comfort.

INTANGIBILITY

The basic difference between services and goods is that services are intangible performances. Because of their intangibility, they cannot be touched, seen, tasted, heard, or felt in the same manner that goods can be sensed. Services cannot be stored and are often easy to duplicate.

Evaluating the quality of services before or even after making a purchase is harder than evaluating the quality of goods because, compared to goods, services tend to exhibit fewer search qualities. A search quality is a characteristic that can be easily assessed before purchase—for instance, the color of an appliance or automobile. At the same time, services tend to exhibit more experience and credence qualities. An experience quality is a characteristic that can be assessed only after use, such as the quality of a meal in a restaurant or the actual experience of a vacation. A credence quality is a characteristic that consumers may have difficulty assessing even after purchase because they do not have the necessary knowledge or experience. Medical and consulting services are examples of services that exhibit credence qualities.

These characteristics also make it harder for marketers to communicate the benefits of an intangible service than to communicate the benefits of tangible goods. Thus, marketers often rely on tangible cues to communicate a service's nature and quality. For example, Travelers' Insurance Company's use of the umbrella symbol helped make tangible the benefit of protection that insurance provides.

The facilities that customers visit, or from which services are delivered, are a critical tangible part of the total service offering. Messages about the organization are communicated to customers through such elements as the decor, the clutter or neatness of service areas, and the staff's manners and dress. Reflecting this idea, the design and development team at Bass Pro Shops believes that in-store displays are not just fixtures, but marketing tools that will attract customers if designed to reflect local culture. So, for example, the Destin, Florida store incorporates indigenous seagulls and swordfish in the chandeliers.[2]

intangibility
The inability of services to be touched, seen, tasted, heard, or felt in the same manner that goods can be sensed.

search quality
A characteristic that can be easily assessed before purchase.

experience quality
A characteristic that can be assessed only after use.

credence quality
A characteristic that consumers may have difficulty assessing even after purchase because they do not have the necessary knowledge or experience.

inseparability
The inability of the production and consumption of a service to be separated. Consumers must be present during the production.

INSEPARABILITY

Goods are produced, sold, and then consumed. In contrast, services are often sold, produced, and consumed at the same time. In other words, their production and consumption are inseparable activities. This inseparability means that, because consumers must be present during the production of services like haircuts or surgery, they are actually involved in the production of the services they buy. That type of consumer involvement is rare in goods manufacturing. Inseparability also means that customers have an opportunity to provide input into their service experience and outcome. For example, individuals getting a haircut can provide feedback during the process so that their hair looks the way they want it to look.

Simultaneous production and consumption also means that services normally cannot be produced in a centralized location and consumed in decentralized locations, as goods typically are. Services are also inseparable from the perspective of the service provider. Thus, the quality of service that firms are able to deliver depends on the quality of their employees.

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HETEROGENEITY

One great strength of McDonald's is consistency. Whether customers order a Big Mac and French fries in Fort Worth, Tokyo, or Moscow, they know exactly what they are going to get. This is not the case with many service providers. Because services have greater heterogeneity, or variability of inputs and outputs, they tend to be less standardized and uniform than goods. For example, physicians in a group practice or barbers in a barber shop differ from one another in their technical and interpersonal skills. A given physician's or barber's performance may even vary depending on time of day, physical health, or some other factor. Because services tend to be labor-intensive, and production and consumption are inseparable, consistency and quality control can be hard to achieve.

Standardization and training help increase consistency and reliability. Limited-menu restaurants like Pizza Hut and KFC offer customers high consistency from one visit to the next because of standardized preparation procedures. Another way to increase consistency is to mechanize the process. Banks have reduced the inconsistency of teller services by providing automated teller machines (ATMs). Automatic coin receptacles and electronic toll collection systems such as E-Z Pass have replaced human collectors on toll roads.

REVIEW LEARNING OUTCOME

LO 2 Discuss the differences between services and goods

Intangible
Inseparable
Heterogeneous
Perishable

PERISHABILITY

The fourth characteristic of services is their perishability, which means that they cannot be stored, warehoused, or inventoried. An empty hotel room or airplane seat produces no revenue that day. The revenue is lost. Yet service organizations are often forced to turn away full-price customers during peak periods.

One of the most important challenges in many service industries is finding ways to synchronize supply and demand. The philosophy that some revenue is better than none has prompted many hotels to offer deep discounts on weekends and during the off-season and has prompted airlines to adopt similar pricing strategies during off-peak hours. Car rental agencies, movie theaters, and restaurants also use discounts to encourage demand during non peak periods.

LO 3
Service Quality

Because of the four unique characteristics of services, service quality is more difficult to define and measure than is the quality of tangible goods. Business executives rank the improvement of service quality as one of the most critical challenges facing them today. The Walt Disney Company's 50,000 employees consistently deliver superior service, which has kept it ranked as an elite service organization for over a decade. Other companies such as Nordstrom, Southwest Airlines and Build-A Bear Workshop also provide exceptional customer service. Everything these companies do reflects their commitment to offering customers a quality service experience.[3] Exhibit 12.1 shows the top 10 ranked Customer Service Elite companies in the U.S.. Research has shown that customers evaluate service quality by the following five components:[4]

- *Reliability*: the ability to perform the service dependably, accurately, and consistently. Reliability is performing the service right the first time. An air

heterogeneity
The variability of the inputs and outputs of services, which causes services to tend to be less standardized and less uniform than goods.

perishability
The inability of services to be stored, warehoused, or inventoried.

reliability
The ability to perform a service dependably, accurately, and consistently

traveler who gets to the destination on time with his or her luggage intact has experienced reliable service. This component has been found to be the one most important to consumers.

- *Responsiveness*: the ability to provide prompt service. Examples of responsiveness include calling the customer back quickly, serving lunch fast to someone who is in a hurry, or mailing a transaction slip immediately. The ultimate in responsiveness is offering service 24 hours a day, seven days a week. For example, Zappos.com, a successful online shoe company, keeps its warehouse open 24/7 so that customers can order shoes at 11 P.M. and still get next-day delivery.[5]
- *Assurance*: the knowledge and courtesy of employees and their ability to convey trust. Skilled employees who treat customers with respect and make customers feel that they can trust the firm to exemplify assurance.

- *Empathy*: caring, individualized attention to customers. Firms whose employees recognize customers, call them by name, and learn their customers' specific requirements are providing empathy. Ritz-Carlton, a service company that has twice won the prestigious Malcolm Baldrige National Quality Award, has a rigorous training program for its employees. For example, bellhops have to learn 28 steps to greeting a guest that includes offering a warm, sincere greeting and using the guest's name when possible.
- *Tangibles*: the physical evidence of the service. The tangible parts of a service include the physical facilities, tools, and equipment used to provide the service, such as a doctor's office or an ATM, and the appearance of personnel. For example, Enterprise Rent-A-Car has strict dress codes for its employees. Female employees have 30 guidelines including that pants must be creased, skirts must not be shorter than two inches above the knee, and legs must be in stockings. Male employees have to follow 26 dress rules, including dress shirts with coordinated ties and no beards. In fact, "distinctive professional dress" is mentioned in Enterprise's written founding values. Hospitals have found that improving their layouts and looks can translate into better health for their patients. After the Barbara Ann Karmanos Cancer Institute in Detroit was renovated, using soft colors, warm indirect lighting, wider hallways and doors, and pullout sofas for visitors, hospital administrators found that patients dealt more effectively with their pain than they had before the remodeling.[6]

Overall service quality is measured by combining customers' evaluations for all five components.

THE GAP MODEL OF SERVICE QUALITY

A model of service quality called the gap model identifies five gaps that can cause problems in service delivery and influence customer evaluations of service quality.[7] These gaps are illustrated in Exhibit 12.2:

- *Gap 1*: the gap between what customers want and what management thinks customers want. This gap results from a lack of understanding or a misinterpretation of the customers' needs, wants, or desires. A firm that does little or no customer satisfaction research is likely to experience this gap. An important step in closing gap 1 is to keep in touch with what customers want by doing research on customer needs and customer satisfaction. Wachovia Bank chairman Ken Thompson holds monthly meetings with his senior managers to go over the results of independent studies that measure customer-employee interactions. Some of this data is gathered from follow up surveys taken at local branches where customers may have given a teller or manager a low service score.[8]

responsiveness
The ability to provide prompt service.

assurance
The knowledge and courtesy of employees and their ability to convey trust.

empathy
Caring, individualized attention to customers.

tangibles
The physical evidence of a service, including the physical facilities, tools, and equipment used to provide the service.

gap model
A model identifying five gaps that can cause problems in service delivery and influence customer evaluations of service quality.

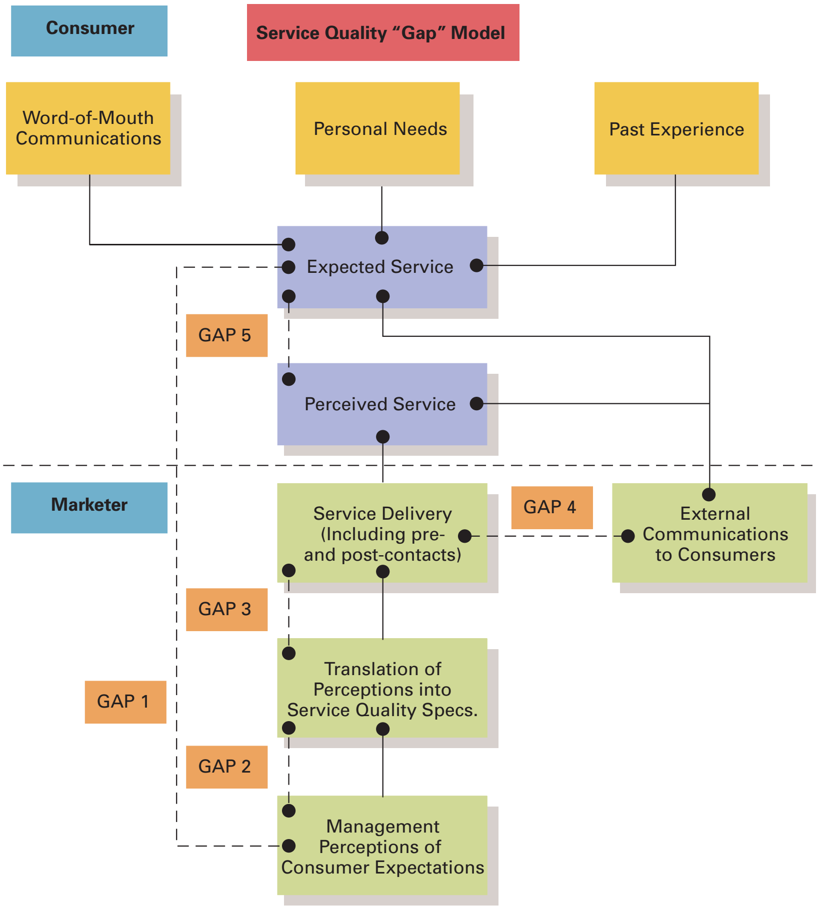
Exhibit 12.1
The Top 10 Customer Service Elite

1. USAA
2. Four Seasons Hotels
3. Cadillac
4. Nordstrom
5. Wegmans Food Markets
6. Edward Jones
7. Lexus
8. UPS
9. Enterprise Rent-a-Car
10. Starbucks

SOURCE: Jena McGregor, "Customer Service Champs," *Business Week*, March 5, 2007, p 54. Reprinted by special permission, © 2007 The McGraw-Hill Companies, Inc.

Exhibit 12.2

Gap Model of Service Quality



SOURCE: Valarie A. Zeithaml, Mary Jo Bitner, and Dwayne Gremler, "Services Marketing", 4/e, © 2006 (New York: McGraw-Hill, 2006).

- Gap 2: the gap between what management thinks customers want and the quality specifications that management develops to provide the service. Essentially, this gap is the result of management's inability to translate customers' needs into delivery systems within the firm. For example, Kentucky Fried Chicken once rated its managers' success according to "chicken efficiency," or how much chicken they threw away at the end of the night. Customers who came in late at night would either have to wait for chicken to be cooked or settle for chicken several hours old. The "chicken efficiency" measurement did not take customers into account.

- *Gap 3*: the gap between the service quality specifications and the service that is actually provided. If both gaps 1 and 2 have been closed, then gap 3 is due to the inability of management and employees to do what should be done. Poorly trained or poorly motivated workers can cause this gap. Management needs to ensure that employees have the skills and the proper tools to perform their jobs. Other techniques that help to close gap 3 are training employees so they know what management expects, encouraging teamwork, and hiring employees with the proper attitude. For example, when recruiting hotel employees, the Four Seasons looks for attitudes that reflect kindness, helpfulness, a genuine desire to see other people happy, and pride in doing things well.[9]

- *Gap 4*: the gap between what the company provides and what the customer is told it provides. This is clearly a communication gap. It may include misleading or deceptive advertising campaigns promising more than the firm can deliver or doing "whatever it takes" to get the business. To close this gap, companies need to create realistic customer expectations through honest, accurate communication about what the firms can provide.

- *Gap 5*: the gap between the service that customers receive and the service they want. This gap can be positive or negative. For example, if a patient expects to wait 20 minutes in the physician's office before seeing the physician but waits only 10 minutes, the patient's evaluation of service quality will be high. However, a 40-minute wait would result in a lower evaluation. Research has found that customer expectations of service across 35 major industries rose 4.5 percent over the previous year, while the average ability of firms in those industries to keep up with those expectations dropped by 9.2 percent. Consumers generally have low expectations for service from credit card issuers, banks, fast food restaurants, and wireless providers. By contrast, they have high expectations from airlines.[10] Exhibit 12.3 shows the service expectations and actual service delivery scores for 11 industries.

Exhibit 12.3

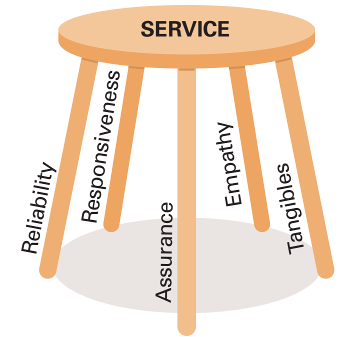
Gaps Between Customer Expectations and Service Delivery

	Expectations Index	Delivery Index
Airlines	145	109
Banks	124	108
Car Rental Companies	161	113
Credit Cards	116	114
Hotels	126	109
Insurance Companies	124	106
Parcel Delivery	124	111
Quick Service Restaurants	116	105
Retail	140	111
Wireless Providers	124	106

SOURCE: From 2006 Brand Keys Index as reported in Michael Applebaum, "One Tough Customer", 'BrandWeek', March 19, 2007, pp. 19–22. Brandweek article used with permission of Nielsen Business Media, Inc.

REVIEW LEARNING OUTCOME

LO 3 Describe the components of service quality and the gap model of service quality



When one or more of these gaps are large, service quality is perceived as low. As the gaps shrink, service quality improves. For instance, Four Seasons has excelled in closing gap 3. Not only does this hotel firm give its employees thorough training, it puts potential employees through a comprehensive screening process to match their skills with positions for which they are naturally inclined. Highly trained and motivated employees are what sets Southwest airlines apart from the competition, For example, after a five-hour delay on a Southwest Airlines plane, the pilot walked the aisles answering questions and offering constant updates while flight attendants kept up with the news on connecting flights. Within a couple of days of after the plane arrived, Southwest sent fliers a letter with an apology that included vouchers for two free round tickets.[11]

LO4 Marketing Mixes for Services

Services' unique characteristics—intangibility, inseparability of production and consumption, heterogeneity, and perishability—make marketing more challenging. Elements of the marketing mix (product, place, promotion, and pricing) need to be adjusted to meet the special needs created by these characteristics.

PRODUCT (SERVICE) STRATEGY

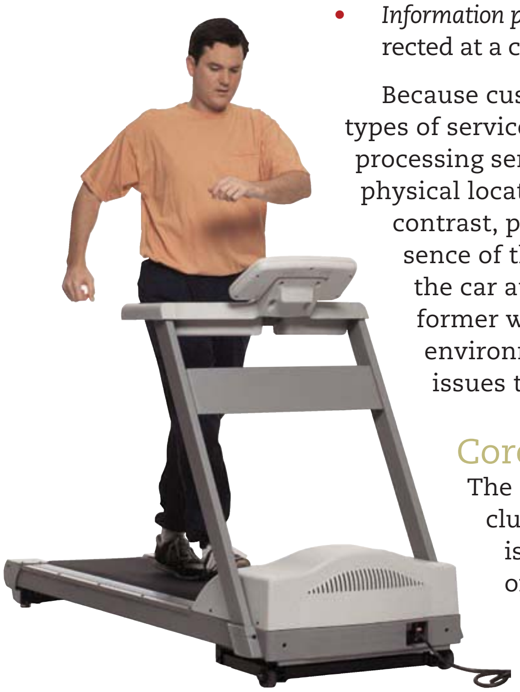
A product, as defined in Chapter 10, is everything a person receives in an exchange. In the case of a service organization, the product offering is intangible and consists in large part of a process or a series of processes. Product strategies for service offerings include decisions on the type of process involved, core and supplementary services, standardization or customization of the service product, and the service mix.

Service as a Process

Two broad categories of things get processed in service organizations: people and objects. In some cases, the process is physical, or tangible, while in others the process is intangible. Based on these characteristics, service processes can be placed into one of four categories:[12]

- *People processing* takes place when the service is directed at a customer. Examples are transportation services, hairstyling, health clubs, and dental and health care.
- *Possession processing* occurs when the service is directed at customers' physical possessions. Examples are lawn care, car repair, dry cleaning, and veterinary services.
- *Mental stimulus processing* refers to services directed at people's minds. Examples are entertainment, spectator sports events, theater performances, and education.

- *Information processing* describes services that use technology or brainpower directed at a customer's assets. Examples are insurance, banking, and consulting.



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Because customers' experiences and involvement differ for each of these types of services, marketing strategies may also differ. For example, people-processing services require customers to enter the *service factory*, which is a physical location, such as an aircraft, a physician's office, or a hair salon. In contrast, possession-processing services typically do not require the presence of the customer in the service factory; the customer may simply leave the car at the garage for repairs, for example. Marketing strategies for the former would therefore focus more on an attractive, comfortable physical environment and employee training on employee-customer interaction issues than would strategies for the latter.

Core and Supplementary Service Products

The service offering can be viewed as a bundle of activities that includes the **core service**, which is the most basic benefit the customer is buying, and a group of **supplementary services** that support or enhance the core service. Exhibit 12.4 illustrates these concepts for overnight stay at a luxury hotel. The core service is overnight rental of a bedroom, which involves people processing. The supplementary services, some of which involve information processing, include reservations, check-ins and check-outs, room service, and meals. Starbucks has added a wireless Internet service called "T-Mobile HotSpot" that enhances its core offering—the Starbucks' experience of high-quality coffee served in a coffeehouse atmosphere. Starbucks is not trying to become an Internet coffeehouse, but to become the "other place" where people want to be connected to the Internet.[13]

core service
The most basic benefit the consumer is buying.

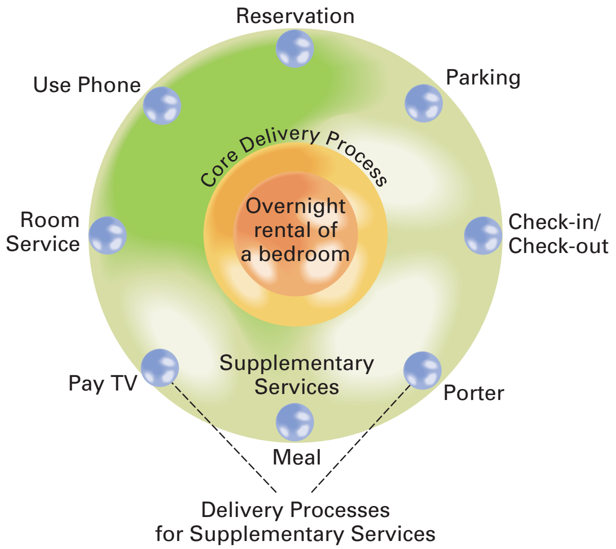
supplementary services
A group of services that support or enhance the core service.

mass customization
A strategy that uses technology to deliver customized services on a mass basis.

In many service industries, the core service becomes a commodity as competition increases. Thus, firms usually emphasize supplementary services to create a competitive advantage. First-class passengers on Virgin Atlantic's flight from Miami to London enjoy seats that convert into flat beds, a bar and bartender, and a chance for a massage. When passengers land, they may shower in a special lounge and then be taken by limousine to their destinations.[14] On the other hand, some firms are positioning themselves in the marketplace by greatly reducing supplementary services. For example, Microtel Inn is an amenity-free hotel concept known as "fast lodging." These low-cost hotels have one- and two-bedroom accommodations and a swimming pool, but no meeting rooms or other services.

Exhibit 12.4

Core and Supplementary Services for a Luxury Hotel



SOURCE: Lovelock, Christopher H.; Wirtz, Jochen, *Services Marketing*, 6th, ©2007. Electronically reproduced by permission of Pearson Education, Inc., Upper Saddle River, New Jersey.

Customization/Standardization

An important issue in developing the service offering is whether to customize or standardize it. Customized services are more flexible and respond to individual customers' needs. They also usually command a higher price. The traditional law firm, which treats each case differently according to the client's situation, offers customized services. Standardized services are more efficient and cost less. Unlike the traditional law firm, for example, Hyatt Legal Services offers low-cost, standardized service "packages" for those with uncomplicated legal needs, such as drawing up a will or mediating an uncontested divorce.

Instead of choosing to either standardize or customize a service, a firm may incorporate elements of both by adopting an emerging strategy called **mass customization**. Mass customization uses technology to deliver customized

PR NEWSFOTO/© NORTHWEST

Making services more personalized is the goal of mass customization. For example, airlines are rolling out personal interactive entertainment systems on airplanes so that passengers can watch movies when they want, rather than only at a set time during the flight.

services on a mass basis, which results in giving each customer whatever she or he asks for.

For example, a feature on Lands' End Web site allows women to define their figures online, receive advice on which swimsuits will flatter their shapes, and mix and match more than 216 combinations of colors and styles. Several airlines are designing services to cater to travelers' individual needs and preferences. Some will serve dinner to passengers when they want to eat it, rather than when the airline wants to serve it. More airlines are offering video-on-demand systems, which let passengers start or stop their movie anytime they want.

The Service Mix

Most service organizations market more than one service. For example, ChemLawn offers lawn care, shrub care, carpet cleaning, and industrial lawn services. Each organization's service mix represents a set of opportunities, risks, and challenges. Each part of the service mix should make a different contribution to achieving the firm's goals. To succeed, each service may also need a different level of financial support.

Designing a service strategy therefore means deciding what new services to introduce to which target market, what existing services to maintain, and what services to eliminate. For example, to increase membership, AAA added financial services, credit cards, and travel perks. Hilton has seven hotel brands that are targeted to different customer segments. For example, the Conrad, in the tower of Hilton's Waldorf Astoria, is one of the fanciest, and most expensive, Hilton hotels. The Hampton Inn is a basic, inexpensive hotel, and Embassy Suites are upscale inns that offer a homelike experience, including kitchen facilities.

PLACE (DISTRIBUTION) STRATEGY

Distribution strategies for service organizations must focus on such issues as convenience, number of outlets, direct versus indirect distribution, location, and scheduling. A key factor influencing the selection of a service provider is *convenience*. Therefore, service firms must offer convenience. Many banks have opened small branches in supermarkets and discount stores like Wal-Mart to make it more convenient for customers to use their services. Restaurants such as Chili's and Macaroni Grill deliver take-out food to customers waiting in their cars. Some doctors are even starting to make house calls to elderly and infirm patients.

An important distribution objective for many service firms is the *number of outlets* to use or the number of outlets to open during a certain time. Generally, the intensity of distribution should meet, but not exceed, the target market's needs and preferences. Having too few outlets may inconvenience customers; having too many outlets may boost costs unnecessarily. Intensity of distribution may also depend on the image desired. Having only a few outlets may make the service seem more exclusive or selective.

The next service distribution decision is whether to distribute services to end users *directly* or *indirectly* through other firms. Because of the intangible nature of services, many service firms have to use direct distribution or franchising. Examples include legal, medical, accounting, and personal-care services. The newest form of direct distribution is the Internet. Most of the major airlines are now using online services to sell tickets directly to consumers, which results in lower distribution

ETHICS in Marketing

Companies Offer Behavioral Targeting Services on the Web

ETHICS

CenturyTel Inc., a Monroe, La., phone company that provides Internet access and long-distance calling services, is facing stiff competition from cell phone companies and cable operators. So to diversify, it's getting into the online-advertising business.

CenturyTel's system allows it to observe and analyze the online activities of its Internet customers, keeping tabs on every Web site they visit. The equipment is made by a Silicon Valley start-up called NebuAd Inc. and installed right into the phone company's network. NebuAd takes the information it collects and offers advertisers the chance to place online ads targeted to individual consumers. NebuAd and CenturyTel get paid whenever a consumer clicks on an ad.

This technique—called behavioral targeting—is more customized than the current method of selling ads online. Today, it's an imperfect process: companies contract with Web sites to monitor which consumers visit them, attaching "cookies," or small pieces of tracking data, to visitors' hard drives so they are recognized when they return. The targeting firms feed the data to Web site owners, who use it to charge premium rates for customized ads. But the information is limited, since the tracking companies can't monitor all of the sites an individual visits.

The newer form of behavioral targeting involves placing gear called "deep-packet inspection boxes" inside an Internet provider's network of pipes and wires. Instead of observing only a select number of Web sites, these boxes can track all of the sites a consumer visits, and deliver more detailed information to potential advertisers. The Internet-service providers often know other information about consumers, such as their names, locations and age and income ranges, which can be very valuable to potential advertisers, especially when combined with Web browsing habits.

However, the idea of matching online and offline information about individual consumers has raised privacy concerns in the past. Many of the major online ad companies have pledged to abide by voluntary standards put forth by the Network Advertising Initiative, an industry group, which call for members to notify consumers that they are being targeted and give them the chance to opt out.

Privacy advocates say transparency is key. "Consumers need to know exactly what is going on and they need to know it at all times," says John Palfrey, executive director of the Berkman Center for the Internet and Society at Harvard University. "Today they say they are using consumer information for ads, but it could be something completely different tomorrow. The ISPs and the companies they are working with need to share as much information as possible."

Some Internet providers are reworking their privacy policies to pre-empt concerns. Many give customers online fact sheets informing them of their new behavioral targeting service along, and ask if they want to participate. If they opt out, the consumers' Internet address is tagged and their Web activity isn't tracked.

For CenturyTel, the new business has already turned into a healthy sideline. The company estimates it will see a 5 percent to 10 percent boost in average revenue per user for its high-speed Internet business, with extra revenue totaling around $2 million a quarter. "We need new revenue streams to survive," says Chris Mangum, vice president of strategic planning of CenturyTel, which notifies its consumers of the behavioral targeting in an online fact sheet and allows them to opt out.

What privacy issues do CenturyTel and other Internet services that provide behavioral targeting raise? Do you think the measures these companies are taking offer enough protection for consumers? What might this technology lead to in the future?

SOURCE: Bobby White, "Watching What You See on the Web", *The Wall Street Journal,* December 6, 2007, B1. Reprinted with permission of *The Wall Street Journal,* © 2007 Dow Jones & Company, Inc. All Rights Reserved Worldwide.

costs for the airline companies. Merrill Lynch offers Merrill Lynch Online, an Internet-based service that connects clients with company representatives. Other firms with standardized service packages have developed indirect channels using independent intermediaries. For example, Bank of America is offering teller services and loan services to customers in small satellite facilities located in Albertson's grocery stores in Texas.

The *location* of a service most clearly reveals the relationship between its target market strategy and its distribution strategy. Reportedly, Conrad Hilton claimed that the three most important factors in determining a hotel's success are "location, location, and location." An interesting location trend has started in the banking industry. In the past few years, banks aggressively directed customers away from branches and toward ATMs and the Internet. In a recent about-face, banks are trying to entice customers back into the branches. For example, Washington Mutual, Inc., based in Seattle, is designing new branches and remodeling old ones to resemble Gap stores.

For time-dependent service providers like airlines, physicians, and dentists, scheduling is often a more important factor. Scheduling is sometimes the most important factor in a customer's choice of airline. MinuteClinic has opened no-appointment-necessary clinics in eight CVS pharmacies in the Atlanta, Georgia area. The goal is to diagnose patients in 15 minutes, start to finish. The drugstore chain rents space to the company under the assumption that patients will pick up their medicines at CVS stores. The advantage for patients is that MinuteClinic is fast and convenient.[15]

PROMOTION STRATEGY

Consumers and business users have more trouble evaluating services than goods because services are less tangible. In turn, marketers have more trouble promoting intangible services than tangible goods. Here are four promotion strategies they can try:

- *Stressing tangible cues:* A tangible cue is a concrete symbol of the service offering. To make their intangible services more tangible, hotels turn down the bedcovers and put mints on the pillows. Insurance companies use symbols like rocks, blankets, umbrellas, and hands to help make their intangible services appear tangible. Merrill Lynch uses a bull to help give its services substance.
- *Using personal information sources:* A personal information source is someone consumers are familiar with (such as a celebrity) or someone they know or can relate to personally. Celebrity endorsements are sometimes used to reduce customers' perceived risk in choosing a service. Service firms may also seek to simulate positive word-of-mouth communication among present and prospective customers by using real customers in their ads.
- *Creating a strong organizational image:* One way to create an image is to manage the evidence, including the physical environment of the service facility, the appearance of the service employees, and the tangible items associated with a service (like stationery, bills, and business cards). For example, McDonald's has created a strong organizational image with its Golden Arches, relatively standardized interiors, and employee uniforms. Another way to create an image is through branding. Disney brands include Disneyland, Disney World, the Disney Channel, and Disney Stores.
- *Engaging in post-purchase communication:* Post-purchase communication refers to the follow-up activities that a service firm might engage in after a customer transaction. Postcard surveys, telephone calls, brochures, and various other types of follow-up show customers that their feedback matters and their patronage is appreciated.

© AP PHOTO/ NATI HARNICK

PRICE STRATEGY

Considerations in pricing a service are similar to the pricing considerations to be discussed in Chapters 18 and 19. However, the unique characteristics of services present two special pricing challenges.

First, in order to price a service, it is important to define the unit of service consumption. For example, should pricing be based on completing a specific service task (cutting a customer's hair), or should it be time based (how long it takes to cut a customer's hair)? Some services include the consumption of goods, such as food and beverages. Restaurants charge customers for food and drink rather than the use of a table and chairs. Some transportation firms charge by distance; others charge a flat rate.

Second, for services that are composed of multiple elements, the issue is whether pricing should be based on a “bundle” of elements or whether each element should be priced separately. A bundled price may be preferable when consumers dislike having to pay “extra” for every part of the service (for example, paying extra for baggage or food on an airplane), and it is simpler for the firm to administer. For instance, many wireless firms offer basic communications packages that include telephone time, Internet access, and text messaging, all for one price. Alternatively, customers may not want to pay for service elements they do not use. Many furniture stores now have “unbundled” delivery charges from the price of the furniture. Customers who wish to can pick up the furniture at the store, saving on the delivery fee.

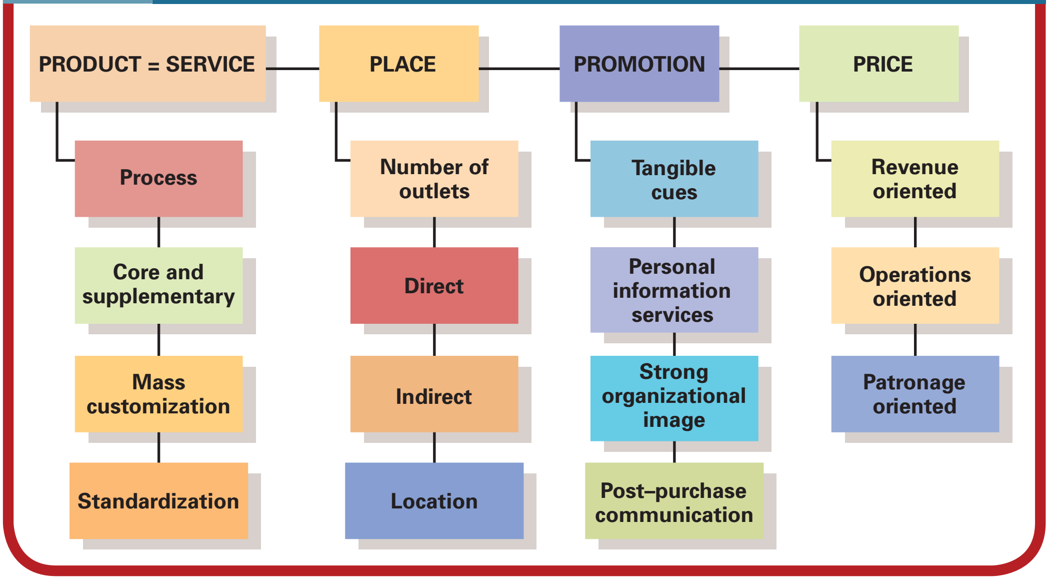
Marketers should set performance objectives when pricing each service. Three categories of pricing objectives have been suggested:[16]

- *Revenue-oriented pricing* focuses on maximizing the surplus of income over costs. A limitation of this approach is that determining costs can be difficult for many services.
- *Operations-oriented pricing* seeks to match supply and demand by varying prices. For example, matching hotel demand to the number of available rooms can be achieved by raising prices at peak times and decreasing them during slow times.
- *Patronage-oriented pricing* tries to maximize the number of customers using the service. Thus, prices vary with different market segments’ ability to pay, and methods of payment (such as credit) are offered that increase the likelihood of a purchase.

A firm may need to use more than one type of pricing objective. In fact, all three objectives probably need to be included to some degree in a pricing strategy, although the importance of each type may vary depending on the type of service provided, the prices that competitors are charging, the differing ability of various customer segments to pay, or the opportunity to negotiate price. For customized services (for example, legal services and construction services), customers may also have the ability to negotiate a price.

REVIEW LEARNING OUTCOME

LO4 Develop marketing mixes for services



This E*Trade advertisement encourages consumers to sign up for the company's membership service by offering a free portfolio review to new users. The ad also provides a message to existing users about the benefits of the company's services.

LO5

Relationship Marketing in Services

Many services involve ongoing interaction between the service organization and the customer. Thus, they can benefit from relationship marketing, the strategy described in Chapter 1, as a means of attracting, developing, and retaining customer relationships. The idea is to develop strong loyalty by creating satisfied customers who will buy additional services from the firm and are unlikely to switch to a competitor. Satisfied customers are also likely to engage in positive word-of-mouth communication, thereby helping to bring in new customers.

Many businesses have found that it is more cost-effective to hang on to the customers they have than to focus only on attracting new ones. A bank executive, for example, found that increasing customer retention by 2 percent can have the same effect on profits as reducing costs by 10 percent.

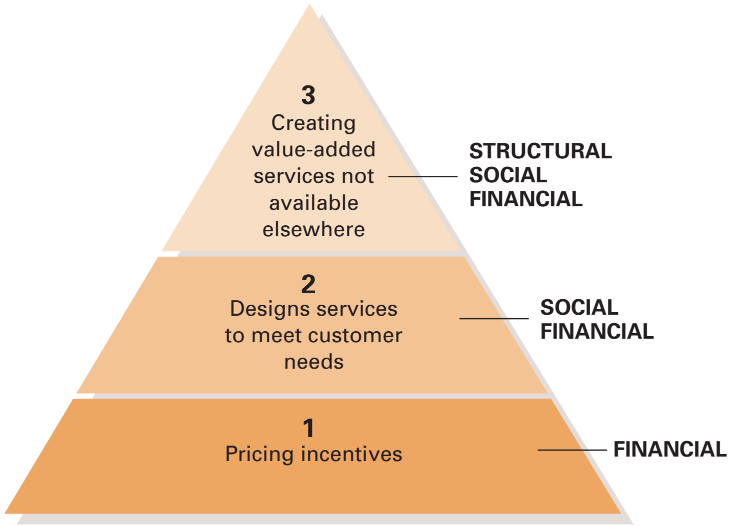
Services that purchasers receive on a continuing basis (for example, cable TV, banking, insurance) can be considered membership services. This type of service naturally lends itself to relationship marketing. When services involve *discrete transactions* (any one-at-a-time sale, such as a movie theater ticket, a meal at a restaurant, or public transportation fare), it may be more difficult to build membership-type relationships with customers. Nevertheless, services involving discrete transactions may be transformed into membership relationships using marketing tools. For example, the service could be sold in bulk (for example, a theater series subscription or a commuter pass on public transportation). Or a service firm could offer special benefits to customers who choose to register with the firm (for example, loyalty programs for hotels, airlines, and car rental firms). The service firm that has a more formalized relationship with its customers has an advantage because it knows who its customers are and how and when they use the services offered.[17]

It has been suggested that relationship marketing can be practiced at three levels:[18]

- *Level 1:* The firm uses pricing incentives to encourage customers to continue doing business with it. Examples include the frequent flyer programs offered by many airlines and the free or discounted travel services given to frequent hotel guests. This level of relationship marketing is the least effective in the long term because its price-based advantage is easily imitated by other firms.
- *Level 2:* This level of relationship marketing also uses pricing incentives but seeks to build social bonds with customers. The firm stays in touch with customers, learns about their needs, and designs services to meet those needs. 1-800-FLOWERS, for example, developed an online Gift Reminder Program. Customers who reach the company via its Web site can register unlimited birthdays, anniversaries, or other special occasions. Five days before each occasion and at their request, 1-800-FLOWERS sends them an e-mail reminder. Level 2 relationship marketing has a higher potential for keeping the firm

REVIEW LEARNING OUTCOME

LO5 Discuss relationship marketing in services



ahead of the competition than does level 1 relationship marketing.

- *Level 3*: At this level, the firm again uses financial and social bonds but adds structural bonds to the formula. Structural bonds are developed by offering value-added services that are not readily available from other firms. Hertz's #1 Club Gold program allows members to call and reserve a car, board a courtesy bus at the airport, tell the driver their name, and get dropped off in front of their car. Hertz also starts up the car and turns on the air conditioning or heat, depending on the temperature. Marketing programs like this one have the strongest potential for sustaining long-term relationships with customers.

LO6 Internal Marketing in Service Firms

internal marketing
Treating employees as customers and developing systems and benefits that satisfy their needs.

Services are performances, so the quality of a firm's employees is an important part of building long-term relationships with customers. Employees who like their jobs and are satisfied with the firm they work for are more likely to deliver superior service to customers. In other words, a firm that makes its employees happy has a better chance of keeping its customers coming back. Studies show that replacing an employee costs roughly 1.5 times a year's pay. Also, companies with highly committed employees have been found to post sharply higher shareholder returns. Thus, it is critical that service firms practice internal marketing, which means treating employees as customers and developing systems and benefits that satisfy their needs.

Companies have instituted a wide variety of programs designed to satisfy employees. Zappos.com, the online shoe company, pays 100 percent of the health insurance premiums for its employees, and every employee gets a free lunch every day.[19] Chipotle Mexican Grill provides its Spanish-speaking employees with English-language instruction, which builds the workers' self-confidence and results in lower employee turnover.[20] At FedEx, a driver explains why he loves the company. If he's cold, he's given gloves. When things get backed up, someone helps. And, he is allowed to set his own route every day.[21] These examples illustrate how service firms can invest in their most important resource—their employees. Exhibit 12.5 shows the top 10 of Fortune's 100 Best Companies to Work For.

REVIEW LEARNING OUTCOME

LO6 Explain internal marketing in services

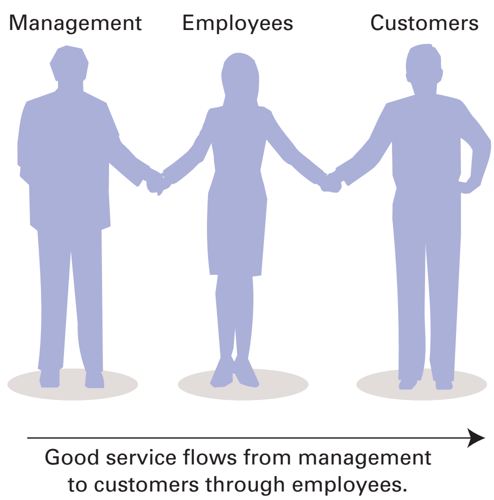


Exhibit 12.5

Top 10 of Fortune's 100 Best Companies to Work For

1. Google
2. Quicken Loans
3. Wegman's Food Markets
4. Edward Jones
5. Genentech
6. Cisco Systems
7. Starbucks
8. Qualcomm
9. Goldman Sachs
10. Methodist Hospital System

SOURCE: "100 Best Companies to Work For: The Rankings", *Fortune*, February 4, 2008, p. 75. © 2008 Time, Inc. All rights reserved.

LO7

Global Issues in Services Marketing

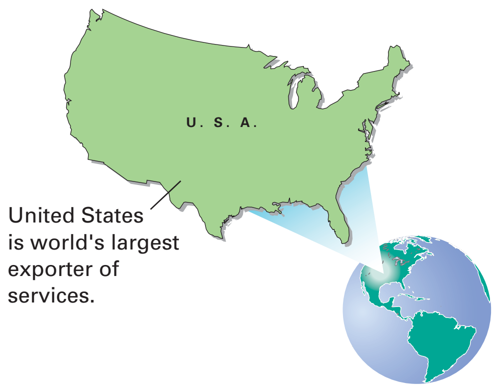
The international marketing of services is a major part of global business, and the United States has become the world's largest exporter of services. Competition in international services is increasing rapidly, however.

To be successful in the global marketplace, service firms must first determine the nature of their core product. Then the marketing mix elements (additional services, place, promotion, pricing, distribution) should be designed to take into account each country's cultural, technological, and political environment.

Because of their competitive advantages, many U.S. service industries have been able to enter the global marketplace. U.S. banks, for example, have advantages in customer service and collections management. The field of construction and engineering services offers great global potential; U.S. companies have vast experience in this industry, so economies of scale are possible for machinery and materials, human resource management, and project management. The U.S. insurance industry has substantial knowledge about underwriting, risk evaluation, and insurance operations that it can export to other countries.

REVIEW LEARNING OUTCOME

LO7 Discuss global issues in services marketing



LO8

Nonprofit Organization Marketing

A nonprofit organization is an organization that exists to achieve some goal other than the usual business goals of profit, market share, or return on investment. Nonprofit organizations share important characteristics with private-sector service firms. Both market intangible products. Both often require the customer to be present during the production process. Both for-profit and nonprofit services vary greatly from producer to producer and from day to day, even from the same producer. Neither for-profit nor nonprofit services can be stored in the way that tangible goods can be produced, saved, and sold at a later date.

Few people realize that nonprofit organizations account for over 20 percent of the economic activity in the United States. The cost of government (i.e., taxes), the predominant form of nonprofit organization, has become the biggest single item in the American family budget—more than housing, food, or health care. Together, federal, state, and local governments collect tax revenues that amount to more than a third of the U.S. gross domestic product. Moreover, they employ nearly one of every five nonagricultural civilian workers. In addition to government entities, nonprofit organizations include hundreds of thousands of private museums, theaters, schools, and churches.

nonprofit organization
An organization that exists to achieve some goal other than the usual business goals of profit, market share, or return on investment.

nonprofit organization marketing
The effort by nonprofit organizations to bring about mutually satisfying exchanges with target markets.

WHAT IS NONPROFIT ORGANIZATION MARKETING?

Nonprofit organization marketing is the effort by nonprofit organizations to bring about mutually satisfying exchanges with target markets. Although these organizations vary substantially in size and purpose and operate in different environments, most perform the following marketing activities:

- Identify the customers they wish to serve or attract (although they usually use another term, such as *clients, patients, members*, or *sponsors*)

- Explicitly or implicitly specify objectives
- Develop, manage, and eliminate programs and services
- Decide on prices to charge (although they use other terms, such as *fees, donations, tuition, fares, fines*, or *rates*)
- Schedule events or programs, and determine where they will be held or where services will be offered
- Communicate their availability through brochures, signs, public service announcements, or advertisements

Often, the nonprofit organizations that carry out these functions do not realize they are engaged in marketing.

UNIQUE ASPECTS OF NONPROFIT ORGANIZATION MARKETING STRATEGIES

Like their counterparts in business organizations, nonprofit managers develop marketing strategies to bring about mutually satisfying exchanges with target markets. However, marketing in nonprofit organizations is unique in many ways—including the setting of marketing objectives, the selection of target markets, and the development of appropriate marketing mixes.

Objectives

In the private sector, the profit motive is both an objective for guiding decisions and a criterion for evaluating results. Nonprofit organizations do not seek to make a profit for redistribution to owners or shareholders. Rather, their focus is often on generating enough funds to cover expenses. The Methodist Church does not gauge its success by the amount of money left in offering plates. The Museum of Science and Industry does not base its performance evaluations on the dollar value of tokens put into the turnstile.

Most nonprofit organizations are expected to provide equitable, effective, and efficient services that respond to the wants and preferences of multiple constituencies. These include users, payers, donors, politicians, appointed officials, the media, and the general public. Nonprofit organizations cannot measure their success or failure in strictly financial terms.

The lack of a financial "bottom line" and the existence of multiple, diverse, intangible, and sometimes vague or conflicting objectives make prioritizing objectives, making decisions, and evaluating performance hard for nonprofit managers. They must often use approaches different from the ones commonly used in the private sector. For example, Planned Parenthood has devised a system for basing salary increases on how employees perform in relation to the objectives they set each year.

Target Markets

Three issues relating to target markets are unique to nonprofit organizations:

- *Apathetic or strongly opposed targets:* Private-sector organizations usually give priority to developing those market segments that are most likely to respond to particular offerings. In contrast, nonprofit organizations must often target those who are apathetic about or strongly opposed to receiving their services, such as vaccinations, family-planning guidance, help for problems of drug or alcohol abuse, and psychological counseling.
- *Pressure to adopt undifferentiated segmentation strategies:* Nonprofit organizations often adopt undifferentiated strategies (see Chapter 8) by default. Sometimes they fail to recognize the advantages of targeting, or an undifferentiated

approach may appear to offer economies of scale and low per capita costs. In other instances, nonprofit organizations are pressured or required to serve the maximum number of people by targeting the average user. The problem with developing services targeted at the average user is that there are few "average" users. Therefore, such strategies typically fail to fully satisfy any market segment.

- *Complementary positioning:* The main role of many nonprofit organizations is to provide services, with available resources, to those who are not adequately served by private-sector organizations. As a result, the nonprofit organization must often complement, rather than compete with, the efforts of others. The positioning task is to identify underserved market segments and to develop marketing programs that match their needs rather than to target the niches that may be most profitable. For example, a university library may see itself as complementing the services of the public library, rather than competing with it.

Product Decisions

There are three product-related distinctions between business and nonprofit organizations:

- *Benefit complexity:* Rather than simple product concepts, like "Fly the friendly skies" or "We make money the old-fashioned way," nonprofit organizations often market complex behaviors or ideas. Examples include the need to exercise or eat right, not to drink and drive, and not to smoke tobacco. The benefits that a person receives are complex, long term, and intangible, and therefore are more difficult to communicate to consumers. St. Jude Children's Research Hospital has developed a simple, yet compelling way to communicate benefits in its slogan "Finding Cures. Saving Children."[22]
- *Benefit strength:* The benefit strength of many nonprofit offerings is quite weak or indirect. What are the direct, personal benefits to you of driving 55 miles per hour, donating blood, or asking your neighbors to contribute money to a charity? In contrast, most private-sector service organizations can offer customers direct, personal benefits in an exchange relationship.
- *Involvement:* Many nonprofit organizations market products that elicit either very low involvement ("Prevent forest fires" or "Don't litter") or very high involvement ("Join the military" or "Stop smoking"). The typical range for private-sector goods is much narrower. Traditional promotional tools may be inadequate to motivate adoption of either low- or high-involvement products.

Nonprofits that request action on the part of consumers must make sure their locations are convenient and accessible. This call2recycle advertisement lists a number of national retailers where consumers can drop off their old batteries for recycling. Consumers will most likely already be visiting these locations to purchase new batteries, making them convenient recycling locations.

Place (Distribution) Decisions

A nonprofit organization's capacity for distributing its service offerings to potential customer groups when and where they want them is typically a key variable in determining the success of those service offerings. For example, most state land-grant universities offer extension programs throughout their state to reach the general public. Many large universities have one or more satellite campus locations to provide easier access for students in other areas. Some educational institutions also offer classes to students at off-campus locations via interactive video technology.

As a global leader in cardiovascular care, Abbott is a sponsor of the American Heart Association's Go Red for Women campaign.

PR NEWSFOTO/© AMERICAN HEART ASSOCIATION

The extent to which a service depends on fixed facilities has important implications for distribution decisions. Obviously, services like rail transit and lake fishing can be delivered only at specific points. Many nonprofit services, however, do not depend on special facilities. Counseling, for example, need not take place in agency offices; it may occur wherever counselors and clients can meet. Probation services, outreach youth programs, and educational courses taught on commuter trains are other examples of deliverable services.

Promotion Decisions

Many nonprofit organizations are explicitly or implicitly prohibited from advertising, thus limiting their promotion options. Most federal agencies fall into this category. Other nonprofit organizations simply do not have the resources to retain advertising agencies, promotion consultants, or marketing staff. However, nonprofit organizations have a few special promotion resources to call on:

- *Professional volunteers:* Nonprofit organizations often seek out marketing, sales, and advertising professionals to help them develop and implement promotion strategies. In some instances, an advertising agency donates its services in exchange for potential long-term benefits. One advertising agency donated its services to a major symphony because the symphony had a blue-ribbon board of directors. Donated services create goodwill, personal contacts, and general awareness of the donor's organization, reputation, and competency.
- *Sales promotion activities:* Sales promotion activities that make use of existing services or other resources are increasingly being used to draw attention to the offerings of nonprofit organizations. Sometimes nonprofit charities even team up with other companies for promotional activities.
- *Public service advertising:* A public service advertisement (PSA) is an announcement that promotes a program of a federal, state, or local government or of a nonprofit organization. Unlike a commercial advertiser, the sponsor of the PSA does not pay for the time or space. Instead, it is donated by the medium. The Advertising Council has developed PSAs that are some of the most memorable advertisements of all time. For example, Smokey the Bear reminded everyone to be careful not to start forest fires.
- *Peer to peer communications:* Some nonprofit agencies have been successful in offering forums for people to share experiences. For example, the March of Dimes Birth Defect Foundation created an online forum at **http://www.shareyourstory.org** to gather real life stories that help spread the word about its mission to prevent birth defects, premature birth, and infant mortality. Families can share their experiences in the form of short stories and blogs.[23]

public service advertisement (PSA)
An announcement that promotes a program of a federal, state, or local government or of a nonprofit organization.

Pricing Decisions

Five key characteristics distinguish the pricing decisions of nonprofit organizations from those of the profit sector:

- *Pricing objectives:* The main pricing objective in the profit sector is revenue or, more specifically, profit maximization, sales maximization, or target return on sales or investment. Many nonprofit organizations must also be concerned about revenue. Often, however, nonprofit organizations seek to either partially or fully defray costs rather than to achieve a profit for distribution to stockholders. Nonprofit organizations also seek to redistribute income—for instance, through taxation and sliding-scale fees. Moreover, they strive to allocate resources fairly among individuals or households or across geographic or political boundaries.
- *Nonfinancial prices:* In many nonprofit situations, consumers are not charged a monetary price but instead must absorb nonmonetary costs. The importance of those costs is illustrated by the large number of eligible citizens who do not take advantage of so-called free services for the poor. In many public assistance programs, about half the people who are eligible don't participate. Nonmonetary costs consist of the opportunity cost of time, embarrassment costs, and effort costs.
- *Indirect payment:* Indirect payment through taxes is common to marketers of "free" services, such as libraries, fire protection, and police protection. Indirect payment is not a common practice in the profit sector.
- *Separation between payers and users:* By design, the services of many charitable organizations are provided for those who are relatively poor and largely paid for by those who are better off financially. Although examples of separation between payers and users can be found in the profit sector (such as insurance claims), the practice is much less prevalent.
- *Below-cost pricing:* An example of below-cost pricing is university tuition. Virtually all private and public colleges and universities price their services below full cost.

REVIEW LEARNING OUTCOME

LO8 Describe nonprofit organization marketing

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percentage of U.S. employment influence by the service sector > **81**

50,000 < service employees at the Walt Disney Company

dress-code guidelines for female Enterprise Rent-A-Car employees > **30**

216 < swimsuit combinations available on the Lands' End Web site

percentage of U.S. economic activity generated by nonprofit organizations > **20**

5 < possible gaps in the gap model of service delivery

minutes the MinuteClinic hopes to spend diagnosing each patient > **15**

Review and Applications

LO 1 **Discuss the importance of services to the economy.** The service sector plays a crucial role in the U.S. economy, employing more than 80 percent of the workforce and accounting for a similar percentage of the gross domestic product.

1.1 To keep track of how service employment is affecting the U.S. economy, go to **http://www.bls.gov/bdm/home.html**. Look at the right sidebar, which gives the latest numbers for Business Employment Dynamics. What trends to you see? Do the numbers support the information from the chapter?

LO 2 **Discuss the differences between services and goods. Services are distinguished by four characteristics.** Services are intangible performances in that they lack clearly identifiable physical characteristics, making it difficult for marketers to communicate their specific benefits to potential customers. The production and consumption of services occur simultaneously. Services are heterogeneous because their quality depends on such elements as the service provider, individual consumer, location, and so on. Finally, services are perishable in the sense that they cannot be stored or saved. As a result, synchronizing supply with demand is particularly challenging in the service industry.

2.1 Assume that you are a manager of a bank branch. Write a list of the implications of intangibility for your firm.

2.2 Over 25 years ago, Tim and Nina Zagat began publishing leisure guides containing reviews of restaurants. Today, the renowned *Zagat* guides still contain reviews of restaurants, but they also rate hotels, entertainment, nightlife, movies, shopping, and even music. Go to **http://www.zagat.com.** In your opinion, are *Zagat* survey guides goods or services? Explain your reasoning.

LO 3 **Describe the components of service quality and the gap model of service quality.** Service quality has five components: reliability (ability to perform the service dependably, accurately, and consistently), responsiveness (providing prompt service), assurance (knowledge and courtesy of employees and their ability to convey trust), empathy (caring, individualized attention), and tangibles (physical evidence of the service).

The gap model identifies five key discrepancies that can influence customer evaluations of service quality. When the gaps are large, service quality is low. As the gaps shrink, service quality improves. Gap 1 is found between customers' expectations and management's perceptions of those expectations. Gap 2 is found between management's perception of what the customer wants and specifications for service quality. Gap 3 is found between service quality specifications and delivery of the service. Gap 4 is found between service delivery and what the company promises to the customer through external communication. Gap 5 is found between customers' service expectations and their perceptions of service performance.

3.1 Analyze a recent experience that you have had with a service business (for example, hairdresser, movie theater, dentist, restaurant, car repair) in terms of your expectations and perceptions about each of the five components of service quality.

LO 4 **Develop marketing mixes for services.** "Product" (service) strategy issues include what is being processed (people, possessions, mental stimulus, information), core and supplementary services, customization versus standardization, and the service mix. Distribution decisions involve convenience, number of outlets, direct versus indirect distribution, and scheduling. Stressing tangible cues, using personal sources of information, creating strong organizational images, and engaging in postpurchase communication are effective promotion strategies. Pricing objectives for services can be revenue oriented, operations oriented, patronage oriented, or any combination of the three.

4.1 Form a team with at least two other classmates, and come up with an idea for a new service. Develop a marketing mix strategy for the new service.

LO 5 **Discuss relationship marketing in services.** Relationship marketing in services involves attracting, developing, and retaining customer relationships. There are three levels of relationship marketing: level 1 focuses on pricing incentives; level 2 uses pricing incentives and social bonds with customers; and level 3 uses pricing, social bonds, and structural bonds to build long-term relationships.

5.1 For the new service developed for question 4.1, have the members of the team discuss how they would implement a relationship marketing strategy.

LO6

Explain internal marketing in services. Internal marketing means treating employees as customers and developing systems and benefits that satisfy their needs. Employees who like their jobs and are happy with the firm they work for are more likely to deliver good service.

6.1 Choose a service firm with which you do a lot of business. Write a memo to the manager explaining the importance of internal marketing and outlining the factors internal marketing includes.

6.2 Return to **http://www.zagat.com** and investigate what the site offers. How does *Zagat* propose to help companies with internal services marketing?

LO7

Discuss global issues in services marketing. The United States has become the world's largest exporter of services. Although competition is keen, the United States has a competitive advantage because of its vast experience in many service industries. To be successful globally, service firms must adjust their marketing mix for the environment of each target country.

7.1 What issues would you have to think about in going global with the new service that you developed in the questions above? How would you change your marketing mix to address those issues?

LO8

Describe nonprofit organization marketing. Nonprofit organizations pursue goals other than profit, market share, and return on investment. Nonprofit organization marketing facilitates mutually satisfying exchanges between nonprofit organizations and their target markets. Several unique characteristics distinguish nonbusiness marketing strategy, including: a concern with services and social behaviors rather than manufactured goods and profit; a difficult, undifferentiated, and in some ways marginal target market; a complex product that may have only indirect benefits and elicit very low involvement; distribution that may or may not require special facilities depending on the service provided; a relative lack of resources for promotion; and prices only indirectly related to the exchange between the producer and the consumer of services.

8.1 Form a team with two or three classmates. Using the promotion strategies discussed in the nonprofit section of this chapter, develop a promotion strategy for your college or university.

Key Terms

assurance	353	inseparability	351	public service advertisement (PSA)	366
core service	356	intangibility	351	reliability	352
credence quality	351	internal marketing	362	responsiveness	353
empathy	353	mass customization	356	search quality	351
experience quality	351	nonprofit organization	363	service	350
gap model	353	nonprofit organization marketing	363	supplementary services	356
heterogeneity	352	perishability	352	tangibles	353

Exercises

APPLICATION EXERCISE

All people know quality when they see it—or do they? Let's take a look at some goods and services and then think about assessing their quality. For this exercise, work in teams of two to three and discuss each item before determining its final placement.[24]

Activities

1. Using the abbreviations in parentheses, place each of the following products and services along the continuum below: a new car (C), designer jeans (J), car oil change (O), dress dry cleaning (D), haircut (H), tax preparation software (T), college education (E).

   100 percent physical good ______________________________ 100 percent service

2. Once you have placed the items along the continuum, consider how easy it is to assess the quality of each item.

   Easy to assess quality ____________________ Difficult to assess quality

3. What assumptions can you make about the ability to assess the quality of goods compared to services? Is it easier to assess the quality of some goods than others? What about for services?

ETHICS EXERCISE

Web sites such as cancerpage.com and CancerSource.com offer cancer patients sophisticated medical data and advice in exchange for personal information that is then sold to advertisers and business partners and used by the Web sites to create products to sell back to patients. Some argue that cancer patients visiting these sites are willingly exchanging their personal information for the sites' medical information. Others contend that this kind of exchange is unethical.

Questions

1. Is this practice ethical?
2. Does the AMA Statement of Ethics have anything to say about this issue? Go to **http://www.marketingpower.com** and review the statement. Then, write a brief paragraph on what the AMA Statement of Ethics contains that relates to this situation.

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Case Study: Minuteclinic

SERVING THE SICK WHERE THEY SHOP

Susan Lyons woke up on a Saturday morning with all the symptoms of strep throat, but her doctor's office was closed for the weekend. Jeremy Brown struggled to get through his workday because of a sinus infection, but he didn't have time on his lunch break to drive across town to see his family physician. Arun Kumar went to his doctor for a flu shot but was turned away because they had already run out of the vaccine. In the end, all three turned to MinuteClinic for treatment instead.

MinuteClinic healthcare centers are open seven days a week with later hours than traditional doctors have. They don't require appointments and can provide patients with a diagnosis and prescription within 15-45 minutes, tops. The fact that they are located in convenient retail settings, usually attached to a CVS drugstore where the prescription can be filled in one stop, adds to their growing appeal. "It was such a pleasant experience," Arun Kumar says after paying $30 for a flu shot at MinuteClinic, "that I figured that I would be happy to go back there for minor ailments and avoid the long waits at my doctor's office."

MinuteClinic, which opened its first location in 2000, was the pioneer of in-store clinics and an innovator in what industry analysts call the "retailization of healthcare." Considering the growing need for cheaper, more accessible healthcare, it's no surprise that the company is expanding so quickly. CVS acquired MinuteClinic in July 2006 and announced plans to grow from 128 locations to nearly 500 by early 2008.

Staffed by nurse practitioners and physician assistants who specialize in family healthcare, MinuteClinic provides basic medical services for common ailments such as ear infections and strep throat. Some locations also offer vaccines and physicals. An electronic medical records system streamlines the process for each patient by generating educational materials, invoices, and prescriptions at the end of the visit. Electronic records also make it possible to instantly transfer information to the patients' primary physicians. MinuteClinic prices range from about $50-$80, making a visit about half as expensive as one to a doctor's office.

MinuteClinic CEO Michael C. Howe says, "MinuteClinic is an example of how creativity and innovation can be brought to our struggling healthcare system to affect change and make basic care more accessible and affordable for today's consumer." The American Medical Association (AMA) has expressed reservations, however. Board member Dr. Rebecca Patchin explains, "The AMA is concerned about patients who would seek care in a freestanding clinic and have a more serious disease that would not be initially diagnosed or diagnosed quickly." Howe insists they are not trying to replace the traditional family physician, however; they simply want to offer a convenient, low-cost alternative for patients with minor illnesses. Patients exhibiting symptoms outside of the clinic's scope of services or showing signs of a chronic condition are referred elsewhere.

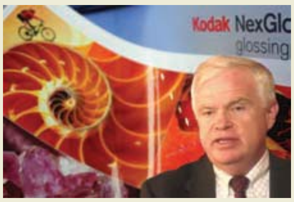
MinuteClinic's ability to handle widespread health emergencies within a community was tested when Minnesota was hit with a string of flu-related deaths in 2007. As a record number of residents sought vaccinations, MinuteClinic quickly put a plan in place to address the crisis and meet the unexpected demand. Instead of boosting staff at all facilities in the Minneapolis area, the company chose a hub-and-spoke approach for better inventory control, offering the shots in only eight MinuteClinic locations. They hired supplemental nursing staff for those clinics and administered up to 300 shots a day in each. The lines became so long that they created children's areas to make the wait easier for families, adding televisions, videos, and coloring books to keep little ones entertained and fostering what Donna Haugland of MinuteClinic describes as "a community-building environment."

CEO Howe praised the good work they did during the flu crisis: "It is amazing what practitioners can do in the right environment and given the chance." Patients agree. The response to the clinics has been overwhelmingly positive. A 2006 Harris Interactive poll reported that 92% of the people who visited a retail clinic were satisfied with its convenience, 89% were satisfied with the quality of care they received, and 80% were satisfied with the cost.

Even the AMA is advising traditional physicians to consider changing their practices to better compete with retail clinics by extending office hours, offering same-day appointments, or even doing away with appointments altogether. AMA Board member Patchin admits, "With their quick and easy access and low prices, the store-based clinics are obviously meeting a need."[25]

Questions

1. Describe how MinuteClinic puts the following promotion strategies to work for them: stressing tangible cues, using personal information sources, creating a strong organizational image, and engaging in post-purchase communication. What else could they try?
2. Are MinuteClinic's services customized or standardized for patients? Do they incorporate any elements of mass customization?
3. In what way did MinuteClinic demonstrate reliability and responsiveness during the flu outbreak in Minnesota? How did it impress customers with tangible physical evidence that the clinics cared about them?
4. How important has MinuteClinic's place (distribution) strategy been to the company's success? Which elements does MinuteClinic focus on with its marketing mix? Why?



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Company Clips

KODAK—REINVENTING THE MIX

You probably think of Kodak as selling only products. In fact, the company has an entire division, the Graphic Communications Group, dedicated to delivering service solutions to business customers. Mark Webber is vice president of worldwide sales partnerships for Kodak's digital printing solutions group, which provides services to the b-to-b (business- to-business) market. In this video, he explains how Kodak creates both digital and analog printing solutions for a wide variety of clients and how the company is taking advantage of new technology to meet evolving customer demands.

Questions

1. Would you describe Kodak's services as customized or standardized? Why?
2. Describe Kodak's services mix.
3. Outline Kodak's pricing strategy for its services.

Marketing & You Results

A high score means you have a positive attitude towards charitable operations and most likely think that nonprofit organizations fulfill an important role in society. However, a high score does not necessarily mean you give more to charity.

Marketing Miscue

The Bigoted Baked Beans

Heinz is a global food company with a large portfolio of worldwide brands, many of which hold the number one or number two market positions in more than 50 countries. The top 15 brands, considered to be "power brands," account for two-thirds of the company's annual sales. The Heinz brand icon is estimated to be worth at least $2.5 billion.

AP PHOTO/RICK RYCROFT

The company's core product categories are: ketchup, condiments, and sauces; frozen foods; infant feeding; and soups, beans, and pasta. World-renowned for its ketchup, the company estimates sales of 650 million bottles of ketchup annually. The company also offers products tailored to local regions. For example in its ketchup, condiments, and sauces core category: Salad Cream in Great Britain; Orlando® in Spain; the Banquette® line in Costa Rica; a banana ketchup called UFC® in the Philippines; ABC® soy sauce in Indonesia; and Jack Daniel's®, Yoshida's®, and Heinz 57® sauces in the United States of America. In total, this core product category sells nearly $2.5 billion worldwide in 140 countries.

The frozen foods core product category represents over $2 billion in sales. One world-renowned brand in this category is the Ore-Ida® brand. Strong brands in the United States are Bagel Bites®, Hot Bites®, Boston Market®, and Smart Ones®. In Britain, favorite Heinz frozen food brands are Weight Watchers®, Jane Asher®, and Linda McCartney®. Heinz® and Wattie's® are standouts in Australia and New Zealand. Prominent brands in the infant feeding food category are Plasmon® in Italy and Farley's® and Farex® in the United Kingdom and India, with Heinz infant feeding products well-known in the United States, Canada, Venezuela, Australia, and China.

It is in the soups, beans, and pasta category however, that Heinz attracted some possibly unwanted attention in 2007. In addition to Honig® dry soup, HAK® vegetables, and KDR® spreads and sprinkles, the company offers Heinz Baked Beanz. In Europe, where almost 40 percent of the company's profits are derived, Heinz Baked Beans comprise one of the company's largest revenue streams. In 1998, the Heinz Baked Beanz line of products was chosen as one of 12 brands that people in Europe thought best represented the final 10 years of the millennium. This put the beans global brand alongside Coca-Cola, McDonalds, The National Lottery, Adidas, Yellow Pages, St. Michael, Bell's Whiskey, Manchester United, BBC, BT, and Vista.

The baked beans product was first imported into the United Kingdom from Canada in 1886. The first British-made Heinz Baked Beanz appeared on store shelves in the UK in 1928. With a recipe known only to four people at any one time, the company makes 1.5 million cans of Heinz Baked Beanz daily. In 1967, the beans were referred to in an advertising campaign with the slogan "Beanz Meanz Heinz." The slogan was much acclaimed and became part of the line of Heinz baked beans sold in the United Kingdom.

The Mean Beanz line is a spicy variety of baked beans launched in the United Kingdom under the product names of Jalfrezi, Mexican, Sweet Chilli, and Tikka. The line was expanded into the Australian marketplace with a new range of flavors. It was this expansion into Australia with the new varieties that raised quite a stir. The new varieties included flavors called Mexican Jackal, Indian Snatcher, and Moroccan Rogue. Unfortunately for Heinz, the product names and the associated depictions on the can labels led to considerable backlash among local ethnic groups.

The ensuing controversy noted that the Australian Mean Beanz line of products tied criminal tendencies to various races. For example, the label on the Indian Snatcher product uses phrasing such as "Danger Level: Volatile if provoked," and "Criminal status: Serving at Long Bay." Local Indian groups in Australia were displeased with this criminal association and suggested that the "racist" beans should be banned. The president of the India Australia Association spoke publicly about the degree of offensiveness in the naming and promotion of the products. One food blog (**http://www.junkfoodblog.com**) took the name association in a different direction and focused on different slang interpretations across the globe. For example, calling someone a jackal in Mexico is apparently a slur, and snatch has various crass connotations.

According to a spokeswoman at Heinz, the product names and campaign were all about edginess and were daring people to try the new exotic flavors. Apparently the Heinz staff in charge of the brand had found the campaign funny. Though the marketing campaign generated critical backlash from some consumers, Heinz had not received complaints about the taste of the products.

Questions

1. How does the brand name, Mean Beanz, serve as a differentiator for the company's line of products?
2. Should Heinz drop the products in Australia?

Critical Thinking Case

Segway—Desirable but not Necessary?

In 1999, Dean Kamen founded a transportation solutions company and, in 2001, the company adopted the name Segway LLC. The Segway name was derived from the word segue, which means to transition smoothly from one state to another. Segway products are designed to empower pedestrians to move quickly, go farther, and evolve into mobile pedestrians on two wheels. The company's first product, the Segway® Personal Transporter (PT), was introduced to the public in late 2001. Positioned as an invention that was going to change the way people move around, the Segway PT was an electric transportation device that utilized the company's patented dynamic stabilization technology.

The dynamic stabilization technology is the brains underlying the company's pedestrian transportation products. The technology is very advanced and has won numerous awards, yet using the final product is relatively straightforward for consumers. The Segway product senses when the user steps on-board and monitors body movement so that the rider can steer and adjust speed by simply leaning forward, backward, right, or left. Essentially, the Segway's patented dynamic stabilization system allows a Segway transporter to balance on just two wheels and provides greater mobility to the pedestrian who is using it.

The company offers products in both the consumer and business-to-business marketplaces. Products for the individual include the I2 (simplest model for easy operation over normal terrain), X2 (enhanced performance on varied terrain with all-terrain tires and wider track), I2 Commuter (specially equipped for commuting and running errands), X2 Adventure (specially equipped for outdoor excursions), and X2 Golf (specially equipped for golf courses with low-pressure tires that barely disturb turf). Products in the business marketplace include the I2, X2, X2 Golf, I2 Cargo (more cargo capacity than the I2 Commuter), I2 Police (specifically designed for police officers and security personnel), and X2 Police (built for patrolling on varied outdoor terrains). The base price for one of these products is reported to start around $5,000.

While the human transporter technology was accepted easily in several cities and municipalities in the United States, it has run into considerable problems in Europe. The problem appears to be that the European Union's laws do not accommodate a new class of vehicle. Before gaining approval for use on sidewalks or streets in EU countries, a vehicle has to have been tested in one of the member states. Once it receives approval in one member state, the vehicle can be operated legally in all other member states. But, it is getting that first approval that has caused problems for Segway, and the company feels that it was completely ambushed in the banning of the product for public roads, bike paths, and walkways.

The Segway is defined as a self-balancing scooter in the EU, powered by electricity with speeds up to 12 mph (20 km/h) and mechanically-propelled. According to the Department for Transport in the United Kingdom, it is a powered vehicle subject to road traffic law. Thus the vehicle requires registration and a vehicle registration license, and the operator needs a driving license and motor insurance. Any vehicle capable of speeds in excess of 4 mph (6 km/h) has to receive European Community Whole Vehicle Type Approval. The absence of rider protection, lights, speedometer, and audible warning devices makes it unlikely that a Segway will gain approval according to current EU laws and regulations. Under the current legal guidelines, a Segway would be classified as a moped, a lightweight motorized bicycle that can be pedaled as well as driven by a low-powered gasoline engine. But, it would not meet the basic technical requirements for a moped since it does not have the mandatory lights or brakes. As such, it would not receive approval as a moped.

The EU does have a licensing classification for self-balancing scooters that is less stringent than the moped classification. However, the Segway does not meet this classification because it can go faster than the 4 mph (6 km/h) restriction. Thus, to gain approval with the current product positioning of traveling quicker and accomplishing more in less time, new legislation to address an unorthodox vehicle such as the Segway will be required in the EU.

Questions

1. What type of product is the Segway?
2. Suggest repositioning strategies that might support growth in the international marketplace.

PART 4

Distribution Decisions

WHAT'S INSIDE

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CHAPTER 13

Marketing Channels

Learning Outcomes

LO 1 Explain what a marketing channel is and why intermediaries are needed

LO 2 Define the types of channel intermediaries and describe their functions and activities

LO 3 Describe the channel structures for consumer and business products and discuss alternative channel arrangements

LO 4 Discuss the issues that influence channel strategy

LO 5 Describe the different channel relationship types and their unique costs and benefits

LO 6 Explain channel leadership, conflict, and partnering

LO 7 Discuss channels and distribution decisions in global markets

LO 8 Identify the special problems and opportunities associated with distribution in service organizations

LO 1

Marketing Channels

marketing channel (channel of distribution) A set of interdependent organizations that ease the transfer of ownership as products move from producer to business user or consumer.

channel members All parties in the marketing channel that negotiate with one another, buy and sell products, and facilitate the change of ownership between buyer and seller in the course of moving the product from the manufacturer into the hands of the final consumer.

The term *channel* is derived from the Latin word *canalis*, which means canal. A marketing channel can be viewed as a large canal or pipeline through which products, their ownership, communication, financing and payment, and accompanying risk flow to the consumer. Formally, a marketing channel (also called a channel of distribution) is a business structure of interdependent organizations that are involved in the process of making a product or service available for use or consumption by end customers or business users. Marketing channels facilitate the physical movement of goods from location to location, thus representing "place" or "distribution" in the marketing mix (product, price, promotion, and place) and encompassing the processes involved in getting the right product to the right place at the right time.

Many different types of organizations participate in marketing channels. Channel members (wholesalers, distributors, and retailers, also sometimes referred to as *intermediaries, resellers,* and *middlemen*) negotiate with one another, buy and sell products, and facilitate the change of ownership between buyer and seller in the course of moving the product from the manufacturer into the hands of the final consumer. As products move through channels, channel members facilitate the distribution process by providing specialization and division of labor, overcoming discrepancies, and providing contact efficiency.

PROVIDING SPECIALIZATION AND DIVISION OF LABOR

According to the concept of *specialization and division of labor,* breaking down a complex task into smaller, simpler ones and allocating them to specialists will create greater efficiency and lower average production costs. Manufacturers achieve economies of scale through the use of efficient equipment capable of producing large quantities of a single product.

Marketing channels can also attain economies of scale through specialization and divi-

Marketing channels aid in overcoming discrepancies of quantity, like the one suggested by this ad for IBM customer relationship management software.

COURTESY OF IBM CORPORATION

Marketing & You

Using the following scale, indicate your opinions on the lines before the items.

1	2	3	4	5
Strongly disagree				Strongly agree

— I would prefer to be a leader.

— I see myself as a good leader.

— I will be a success.

— People always seem to recognize my authority.

— I have a natural talent for influencing people.

— I am assertive.

— I like to have authority over other people.

— I am a born leader.

Now, total your score. Read the chapter and find out what your score means at the end.


© FOODPIX/JUPITER IMAGES

sion of labor by aiding producers who lack the motivation, financing, or expertise to market directly to end users or consumers. In some cases, as with most consumer convenience goods, such as soft drinks, the cost of marketing directly to millions of consumers—taking and shipping individual orders—is prohibitive. For this reason, producers hire channel members, such as wholesalers and retailers, to do what the producers are not equipped to do or what channel members are better prepared to do. Channel members can do some things more efficiently than producers because they have built good relationships with their customers. Therefore, their specialized expertise enhances the overall performance of the channel.

OVERCOMING DISCREPANCIES

Marketing channels also aid in overcoming discrepancies of quantity, assortment, time, and space created by economies of scale in production. For example, assume that Pillsbury can efficiently produce its Hungry Jack instant pancake mix only at a rate of 5,000 units in a typical day. Not even the most ardent pancake fan could consume that amount in a year, much less in a day. The quantity produced to achieve low unit costs has created a discrepancy of quantity, which is the difference between the amount of product produced and the amount an end user wants to buy. By storing the product and distributing it in the appropriate amounts, marketing channels overcome quantity discrepancies by making products available in the quantities that consumers desire.

discrepancy of quantity
The difference between the amount of product produced and the amount an end user wants to buy.

discrepancy of assortment
The lack of all the items a customer needs to receive full satisfaction from a product or products.

temporal discrepancy
A situation that occurs when a product is produced but a customer is not ready to buy it.

spatial discrepancy
The difference between the location of a producer and the location of widely scattered markets.

Mass production creates not only discrepancies of quantity but also discrepancies of assortment. A discrepancy of assortment occurs when a consumer does not have all of the items needed to receive full satisfaction from a product. For pancakes to provide maximum satisfaction, several other products are required to complete the assortment. At the very least, most people want a knife, fork, plate, butter, and syrup. Others might add orange juice, coffee, cream, sugar, eggs, and bacon or sausage. Even though Pillsbury is a large consumer-products company, it does not come close to providing the optimal assortment to go with its Hungry Jack pancakes. To overcome discrepancies of assortment, marketing channels assemble in one place many of the products necessary to complete a consumer's needed assortment.

A temporal discrepancy is created when a product is produced, but a consumer is not ready to buy it. Marketing channels overcome temporal discrepancies by maintaining inventories in anticipation of demand. For example, manufacturers of seasonal merchandise, such as Christmas or Halloween decorations, are in operation all year even though consumer demand is concentrated during certain months of the year.

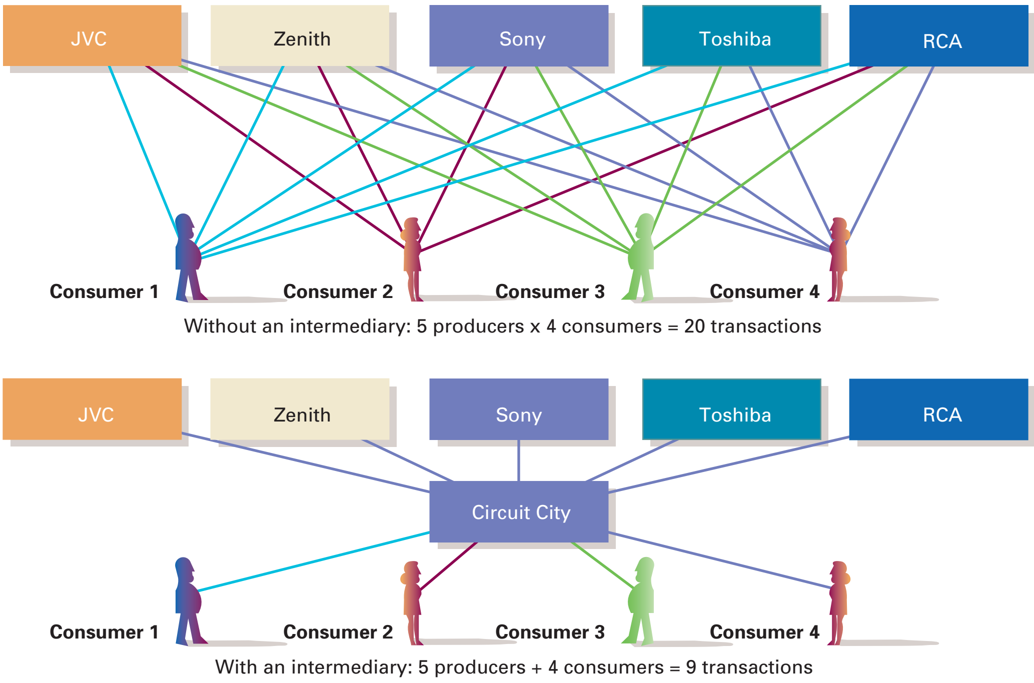
Furthermore, because mass production requires many potential buyers, markets are usually scattered over large geographic regions, creating a spatial discrepancy. Often global, or at least nationwide, markets are needed to absorb the outputs of mass producers. Marketing channels overcome spatial discrepancies by making products available in locations convenient to consumers. For example, if all the Hungry Jack pancake mix is produced in Boise, Idaho, then Pillsbury must use an intermediary to distribute the product to other regions of the United States. Consumers elsewhere would be unwilling to drive to Boise to purchase pancake mix.

PROVIDING CONTACT EFFICIENCY

The third need fulfilled by marketing channels is that they provide contact efficiency. Marketing channels provide contact efficiencies by reducing the number of stores customers must shop in to complete their purchases. Think about how much time

Exhibit 13.1

How Marketing Channels Reduce the Number of Required Transactions



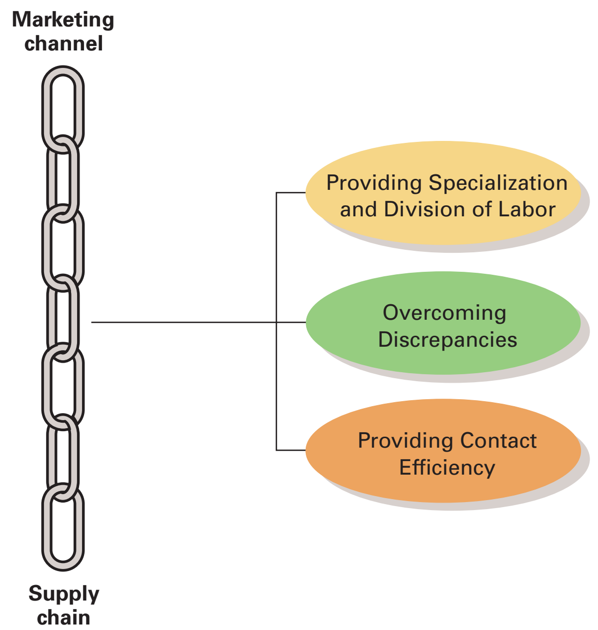
you would spend shopping if supermarkets, department stores, and shopping malls did not exist. For example, suppose you had to buy your milk at a dairy and your meat at a stockyard. Imagine buying your eggs and chicken at a hatchery and your fruits and vegetables at various farms. You would spend a great deal of time, money, and energy just shopping for a few groceries. Channels simplify distribution by cutting the number of transactions required to get products from manufacturers to consumers and making an assortment of goods available in one location. In addition, many consumers in recent years have begun shopping using a multi-channel approach whereby they view products online, in catalogues, and in the brick-and-mortar retail outlet. Savvy retailers are capitalizing on these additional customer contacts by segmenting customers according to buying versus simply shopping channels and providing consistent messages to customers regardless of channel choice.[1]

Consider the example illustrated in Exhibit 13.1. Four consumers each want to buy a television set. Without a retail intermediary like Circuit City, television manufacturers JVC, Zenith, Sony, Toshiba, and RCA would each have to make four contacts to reach the four buyers who are in the target market, for a total of 20 transactions. However, when Circuit City acts as an intermediary between the producer and consumers, each producer has to make only one contact, reducing the number of transactions to 9. Each producer sells to one retailer rather than to four consumers. In turn, consumers buy from one retailer instead of from five producers.

Contact efficiency is being enhanced even more by information technology. Better information on product availability and pricing increasingly is reducing the need for consumers to

REVIEW LEARNING OUTCOME

LO 1 Explain what a marketing channel is and why intermediaries are needed



actually shop for bargains or view ads in a traditional manner. By making information on products and services easily accessible over the Internet, Google, Yahoo, and similar information assemblers are becoming the starting points for finding and buying products and services. As they cull and organize huge digital warehouses of news, images, traffic and weather reports, and information on automobiles, real estate, and other consumer products, inefficiencies will be reduced, as will prices. These developments are revolutionizing marketing channels and benefiting consumers because shoppers can find out where the best bargains are without having to search for them.[2]

LO 2

Channel Intermediaries and Their Functions

retailer
A channel intermediary that sells mainly to consumers.

merchant wholesaler
An institution that buys goods from manufacturers and resells them to businesses, government agencies, and other wholesalers or retailers and that receives and takes title to goods, stores them in its own warehouses, and later ships them.

agents and brokers
Wholesaling intermediaries who do not take title to a product but facilitate its sale from producer to end user by representing retailers, wholesalers, or manufacturers.

Intermediaries in a channel negotiate with one another, facilitate the change of ownership between buyers and sellers, and physically move products from the manufacturer to the final consumer. The most prominent difference separating intermediaries is whether they take title to the product. *Taking title* means they own the merchandise and control the terms of the sale—for example, price and delivery date. Retailers and merchant wholesalers are examples of intermediaries that take title to products in the marketing channel and resell them. Retailers are firms that sell mainly to consumers. Retailers will be discussed in more detail in Chapter 15.

Merchant wholesalers are organizations that facilitate the movement of products and services from the manufacturer to producers, resellers, governments, institutions, and retailers. All merchant wholesalers take title to the goods they sell, and most of them operate one or more warehouses where they receive goods, store them, and later reship them. Customers are mostly small- or moderate-sized retailers, but merchant wholesalers also market to manufacturers and institutional clients.

Other intermediaries do not take title to goods and services they market but do facilitate the exchange of ownership between sellers and buyers. Agents and brokers simply facilitate the sale of a product from producer to end user by representing retailers, wholesalers, or manufacturers. Title reflects ownership, and ownership usually implies control. Unlike wholesalers, agents or brokers only facilitate sales and generally have little input into the terms of the sale. They do, however, get a fee or commission based on sales volume. For example, when selling a home, the owner usually hires a real estate agent who then brings potential buyers to see the house. The agent facilitates the sale by bringing the buyer and owner together, but never actually takes ownership of the home.

Variations in channel structures are due in large part to variations in the numbers and types of wholesaling intermediaries. Generally, product characteristics, buyer considerations, and market conditions determine the type of intermediary the manufacturer should use.

- *Product characteristics* that may require a certain type of wholesaling intermediary include whether the product is standardized or customized, the complexity of the product, and the gross margin of the product. For example, a customized product such as insurance is sold through an insurance agent or broker who may represent one or multiple companies. In contrast, a standardized product such as gum is sold through a merchant wholesaler that takes possession of the gum and reships it to the appropriate retailers.
- *Buyer considerations* affecting the wholesaler choice include how often the product is purchased and how long the buyer is willing to wait to receive the product. For example, at the beginning of the school term, a student may be willing to wait a few days for a textbook to get a lower price by ordering online. Thus, this type of product can be distributed directly. But, if the student waits to buy the book until right before an exam and needs the book immediately, it will have to be purchased at the school bookstore.

Exhibit 13.2

Marketing Channel Functions Performed by Intermediaries

Type of Function	Description
Transactional functions	**Contacting and promoting:** Contacting potential customers, promoting products, and soliciting orders **Negotiating:** Determining how many goods or services to buy and sell, type of transportation to use, when to deliver, and method and timing of payment **Risk taking:** Assuming the risk of owning inventory
Logistical Functions	**Physically distributing:** Transporting and sorting goods to overcome temporal and spatial discrepancies **Storing:** Maintaining inventories and protecting goods **Sorting:** Overcoming discrepancies of quantity and assortment by *Sorting out:* Breaking down a heterogeneous supply into separate homogeneous stocks *Accumulating:* Combining similar stocks into a larger homogeneous supply *Allocating:* Breaking a homogeneous supply into smaller and smaller lots ("breaking bulk") *Assorting:* Combining products into collections or assortments that buyers want available at one place
Facilitating Functions	**Researching:** Gathering information about other channel members and consumers **Financing:** Extending credit and other financial services to facilitate the flow of goods through the channel to the final consumer

- *Market characteristics* determining the wholesaler type include how many buyers are in the market and whether they are concentrated in a general location or are widely dispersed. Gum and textbooks, for example, are produced in one location and consumed in many other locations. Therefore, a merchant wholesaler is needed to distribute the products. In contrast, in a home sale, the buyer and seller are localized in one area, which facilitates the use of an agent/broker relationship.

CHANNEL FUNCTIONS PERFORMED BY INTERMEDIARIES

Retailing and wholesaling intermediaries in marketing channels perform several essential functions that make the flow of goods between producer and buyer possible. The three basic functions that intermediaries perform are summarized in Exhibit 13.2.

Transactional functions involve contacting and communicating with prospective buyers to make them aware of existing products and explain their features, advantages, and benefits. Intermediaries in the channel also provide *logistical* functions. Logistics is the efficient and cost-effective forward and reverse flow and storage of goods, services, and related information, into, through, and out of channel member companies. Logistics functions typically include transportation and storage of assets, as well as their sorting, accumulation, consolidation, and/or allocation for the purpose of conforming to customer requirements. For example, grading agricultural products typifies the sorting-out process, while consolidation of many lots of grade A eggs from different sources into one lot illustrates the accumulation process. Supermarkets or other retailers perform the assorting function by assembling thousands of different items that match their customers' desires. Similarly, while large companies typically have direct channels, many small companies depend on wholesalers to promote and distribute their products. For example, small beverage manufacturers like Jones Soda, Honest Tea, and Energy Brands depend on wholesalers to distribute their products in a marketplace dominated by large competitors like Coca-Cola and Pepsi. The management of logistics is a key component of what has come to be known as supply chain management, which is discussed in greater detail in Chapter 14.

logistics
The efficient and cost-effective forward and reverse flow as well as storage of goods, services, and related information, into, through, and out of channel member companies. Logistics functions typically include transportation and storage of assets, as well as their sorting, accumulation, consolidation, and/or allocation for the purpose of meeting customer requirements.

The third basic channel function, *facilitating,* includes research and financing. Research provides information about channel members and consumers by getting answers to key questions: Who are the buyers? Where are they located? Why do they buy? Financing ensures that channel members have the money to keep products moving through the channel to the ultimate consumer.

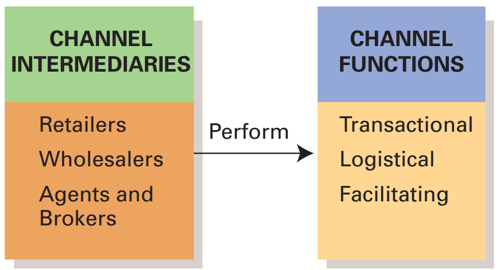
A single company may provide one, two, or all three functions. Consider Kramer Beverage Company, a Coors beer distributor. As a beer distributor, Kramer provides transactional, logistical, and facilitating channel functions. Sales representatives contact local bars and restaurants to negotiate the terms of the sale, possibly giving the customer a discount for large purchases, and arrange for delivery of the beer.

At the same time, Kramer also provides a facilitating function by extending credit to the customer. Kramer merchandising representatives, meanwhile, assist in promoting the beer on a local level by hanging Coors beer signs and posters. Kramer also provides logistical functions by accumulating the many types of Coors beer from the Coors manufacturing plant in Golden, Colorado, and storing them in its refrigerated warehouse. When an order needs to be filled, Kramer then sorts the beer into heterogeneous collections for each particular customer. For example, the local Chili's Grill & Bar may need two kegs of Coors, three kegs of Coors Light, and two cases of Killian's Red in bottles. The beer will then be loaded onto a refrigerated truck and transported to the restaurant. Upon arrival, the Kramer delivery person will transport the kegs and cases of beer into the restaurant's refrigerator and may also restock the coolers behind the bar.

Although individual members can be added to or deleted from a channel, someone must still perform these essential functions. They can be performed by producers, end users or consumers, channel intermediaries such as wholesalers and retailers, and sometimes nonmember channel participants. For example, if a manufacturer decides to eliminate its private fleet of trucks, it must still have a way to move the goods to the wholesaler. This task may be accomplished by the wholesaler, which may have its own fleet of trucks, or by a nonmember channel participant, such as an independent trucking firm. Nonmembers also provide many other essential functions that may at one time have been provided by a channel member. For example, research firms may perform the research function; advertising agencies may provide the promotion function; transportation and storage firms, the physical distribution function; and banks, the financing function.

REVIEW LEARNING OUTCOME

LO 2 Define the types of channel intermediaries and describe their functions and activities



LO 3

Channel Structures

A product can take many routes to reach its final consumer.

Marketers search for the most efficient channel from the many alternatives available. Marketing a consumer convenience good like gum or candy differs from marketing a specialty good like a Mercedes-Benz. The two products require very different distribution channels. Likewise, the appropriate channel for a major equipment supplier like Boeing Aircraft would be unsuitable for an accessory equipment producer like Black & Decker. The next sections discuss the structures of typical marketing channels for consumer and business-to-business products. Alternative channel structures are also discussed.

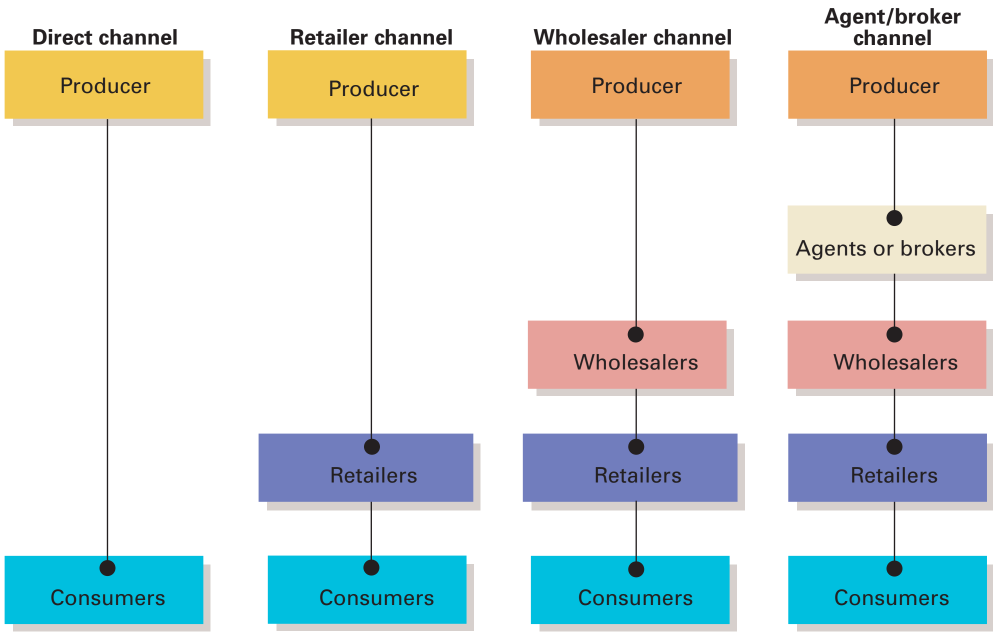
CHANNELS FOR CONSUMER PRODUCTS

direct channel
A distribution channel in which producers sell directly to consumers.

Exhibit 13.3 illustrates the four ways manufacturers can route products to consumers. Producers use the direct channel to sell directly to consumers. Direct marketing activities—including telemarketing, mail-order and catalog shopping, and forms of electronic retailing like online shopping and shop-at-home television networks—are a good example of this type of channel structure. For example, home computer users can purchase Dell computers directly over the telephone or from Dell's Internet Web site. There are no intermediaries. Producer-owned stores and factory outlet stores—like Sherwin-Williams, Polo Ralph Lauren, Oneida, and West Point Pepperell—are other examples of direct channels. Farmers' markets are also direct channels. Direct marketing and factory outlets are discussed in more detail in Chapter 15.

Exhibit 13.3

Marketing Channels for Consumer Products



At the other end of the spectrum, an *agent/broker channel* involves a fairly complicated process. Agent/broker channels are typically used in markets with many small manufacturers and many retailers that lack the resources to find each other. Agents or brokers bring manufacturers and wholesalers together for negotiations, but they do not take title to merchandise. Ownership passes directly to one or more wholesalers and then to retailers. Finally, retailers sell to the ultimate consumer of the product. For example, a food broker represents buyers and sellers of grocery products. The broker acts on behalf of many different producers and negotiates the sale of their products to wholesalers that specialize in foodstuffs. These wholesalers in turn sell to grocers and convenience stores.

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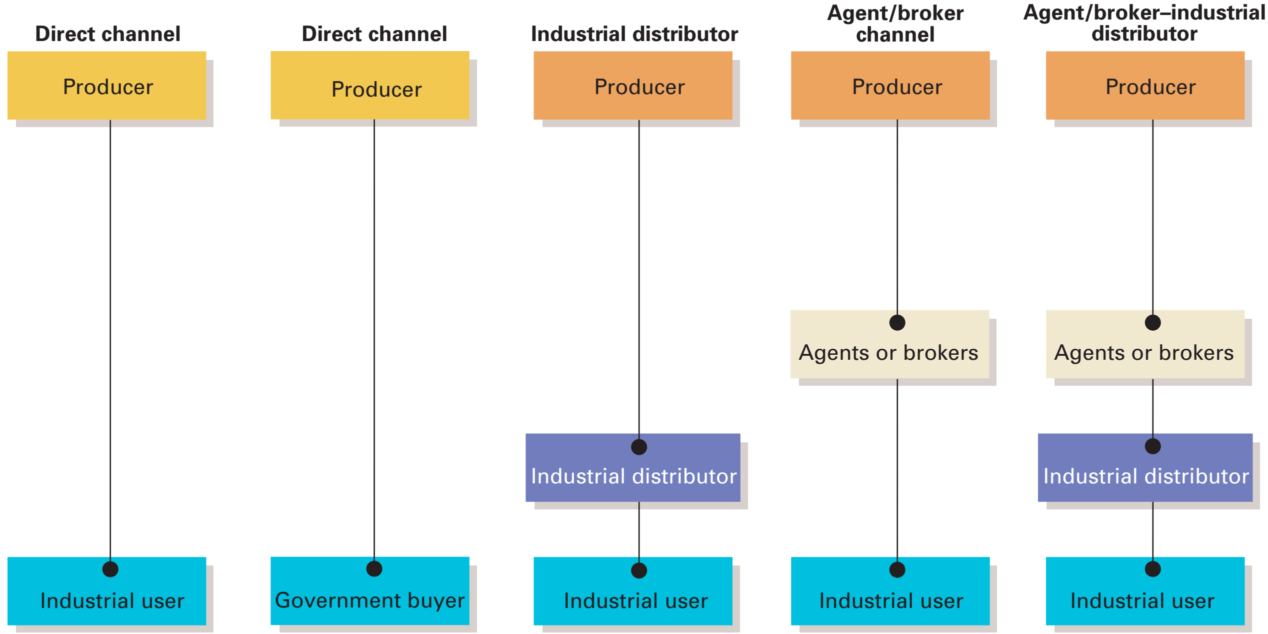
Most consumer products are sold through distribution channels similar to the other two alternatives: the retailer channel and the wholesaler channel. A *retailer channel* is most common when the retailer is large and can buy in large quantities directly from the manufacturer. Wal-Mart, Target, JC Penney, and car dealers are examples of retailers that often bypass a wholesaler. A *wholesaler channel* is commonly used for low-cost items that are frequently purchased, such as candy, cigarettes, and magazines. For example, M&M/Mars sells candies and chocolates to wholesalers in large quantities. The wholesalers then break these quantities into smaller quantities to satisfy individual retailer orders.

CHANNELS FOR BUSINESS AND INDUSTRIAL PRODUCTS

As Exhibit 13.4 on the next page illustrates, five channel structures are common in business and industrial markets. First, direct channels are typical in business and industrial markets. For example, manufacturers buy large quantities of raw materials, major equipment, processed materials, and supplies directly from other manufacturers. Manufacturers that require suppliers to meet detailed technical specifications often prefer direct channels. The direct communication required between DaimlerChrysler and its suppliers, for example, along with the tremendous size of the orders, makes anything but a direct channel impractical. The channel from producer to government buyers is also a direct channel. Since much government buying is done through bidding, a direct channel is attractive. Dell, for example, the

Exhibit 13.4

Channels for Business and Industrial Products



top seller of desktop computers to federal, state, and local government agencies in the United States, sells the computers through direct channels.

Companies selling standardized items of moderate or low value often rely on *industrial distributors*. In many ways, an industrial distributor is like a supermarket for organizations. Industrial distributors are wholesalers and channel members that buy and take title to products. Moreover, they usually keep inventories of their products and sell and service them. Often small manufacturers cannot afford to employ their own sales force. Instead, they rely on manufacturers' representatives or selling agents to sell to either industrial distributors or users.

Today, though, the traditional industrial distributor is facing many challenges. Manufacturers are getting bigger due to growth, mergers, and consolidation. Through technology, manufacturers and customers have access to information that in the past only the distributor had. Consequently, many manufacturers and customers are bypassing distributors and going direct, often via the Internet. The Internet has enabled virtual distributors to emerge and forced traditional industrial distributors to expand their business model. An example of how the Internet has revolutionized industrial distribution is **http://www.pumpbiz.com**, which sells pumps for chemicals, wastewater, sumps, water, coolants, and all other industrial process fluids. Pump types available include centrifugal, diaphragm, vertical, magnetic drive, and metering pumps. The site offers 24/7 purchasing and provides access to information on major manufacturers of pumps, including side-by-side comparisons and reviews; copies of manuals, diagrams, and other installation and repair documentation; warranted installers in the customer's local area; and instant access to past purchasing and related information on a customer's account.[3]

The Internet has also led to the emergence of three other new forms of industrial distribution. Some companies serve as agents that link buyers and sellers and charge a fee. For example, Expedia.com links business travelers to airlines, hotels, and car rental companies. A second form of marketplace has been developed by existing companies looking for a way to drop the intermediary from the channel. For example, the Worldwide Retail Exchange is a marketplace created by 17 major retailers including Target, JCPenney, and Walgreens. Retailers use the exchange to make purchases that in the past would have required telephone, fax, or face-to-face sales calls. Retailers using the exchange estimate they have saved approximately

15 percent in their purchasing costs. Finally, a third type of Internet marketplace is a "private exchange." Private exchanges allow companies to automate their channels while sharing information only with select suppliers. Ace Hardware and Hewlett-Packard, for example, use private exchanges to manage their inventory supplies. Another example is I-textile, which enables companies in the textile business to communicate over a secure online platform to place orders, update information, and standardize transactions.[4]

ALTERNATIVE CHANNEL ARRANGEMENTS

Rarely does a producer use just one type of channel to move its product. It usually employs several different or alternative channels, which include multiple channels, nontraditional channels, and strategic channel alliances.

Multiple Channels

dual distribution (multiple distribution)
The use of two (or more) channels to distribute the same product to target markets.

When a producer selects two (or more) channels to distribute the same product to target markets, this arrangement is called dual distribution (or multiple distribution). As more people have access to the Internet and embrace online shopping, an increasing number of retailers are using multiple channels of distribution. For example, companies such as Limited Brands, which includes The Limited, Express, Victoria's Secret, and Bath and Body Works, sell in-store, online, and through catalogs. Other examples are Sears and Avon. Since Sears purchased Lands' End, a traditional direct business-to-consumer clothing manufacturer, Lands' End products are available in Sears's stores, and Sears credit cards are accepted on the Lands' End Web site. Avon, a direct supplier of health and beauty products for women, offers consumers four alternatives for purchasing products. They can contact a representative in person (the original business model), purchase on the Web, order direct from the company, or pick up products at an Avon Salon & Spa. The Limited, Sears/Lands' End, and Avon, are each distributing identical products to existing markets using more than one channel of distribution.[5]

Nontraditional Channels

Often nontraditional channel arrangements help differentiate a firm's product from the competition. For example, manufacturers may decide to use nontraditional channels such as the Internet, mail-order channels, or infomercials to sell products instead of going through traditional retailer channels. Although nontraditional channels may limit a brand's coverage, they can give a producer serving a niche market a way to gain market access and customer attention without having to establish channel intermediaries. Nontraditional channels can also provide another avenue of sales for larger firms. For example, a London publisher sells short stories through vending machines in the London Underground. Instead of the traditional book format, the stories are printed like folded maps, making them an easy-to-read alternative for commuters.

Kiosks, long a popular method for ordering and registering for wedding gifts, dispersing cash through ATMs, and facilitating airline check-in, are finding new uses. Ethan Allen furniture stores use kiosks as a product locator tool for consumers and salespeople. Kiosks on the campuses of Cheney University allow students to register for classes, see their class schedule and grades, check account balances, and even print transcripts. The general public, when it has access to the kiosks, can use them to gather information about the university.[6]

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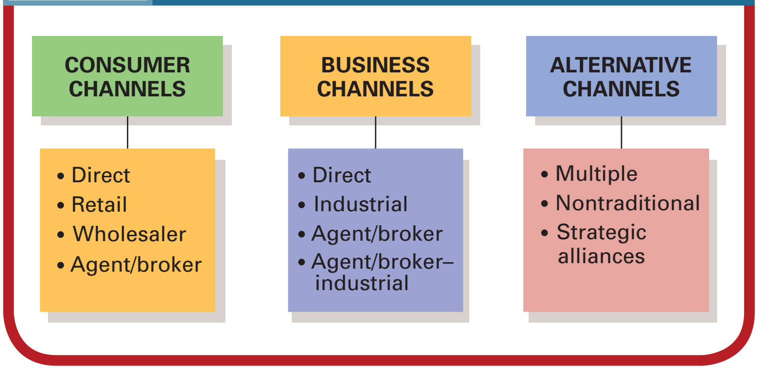
Strategic Channel Alliances

strategic channel alliance
A cooperative agreement between business firms to use the other's already established distribution channel.

Companies often form strategic channel alliances. Such an alliance enables a company to use another manufacturer's already established channel. Alliances are used most often when the creation of marketing channel relationships may be too expensive and time-consuming. Starbucks, the world's premier coffee marketer, uses strategic alliances both domestically and around the world. When Starbucks wanted to develop ready-to-drink (RTD) coffee beverages for supermarkets and other outlets, it decided not to develop a new channel from scratch. Rather, Starbucks signed an agreement with Pepsi to develop and bottle a Starbucks brand of RTD coffee, a category that had been extremely difficult to develop. The resulting Frappuccino and DoubleShot were so successful when they were launched that they were constantly sold out. Today, nearly 15 years since the Pepsi/Starbucks alliance first was forged, Pepsi is still the sole distributor for Starbucks RTD beverages like Frappuccino and DoubleShot, and Starbucks has continued access to the thousands of outlets where Pepsi is sold.[7] Similarly, Accenture and Cisco Systems have formed an alliance to work together in the joint development, marketing, and deployment of global network solutions. The combination of Accenture's network consulting services and Cisco's advanced technology will result in cost savings in asset acquisition and service delivery for their customers.[8] Strategic channel alliances are proving to be more successful for growing businesses than mergers and acquisitions. This is especially true in global markets where cultural differences, distance, and other barriers can prove challenging. For example, Heinz has a strategic alliance with Kagome, one of Japan's largest food companies. The companies are working together to find ways to reduce operating costs while expanding both brands' market presence globally.

REVIEW LEARNING OUTCOME

LO3 Describe the channel structures for consumer and business products and discuss alternative channel arrangements



LO4 Making Channel Strategy Decisions

Devising a marketing channel strategy requires several critical decisions. Managers must decide what role distribution will play in the overall marketing strategy. In addition, they must be sure that the channel strategy chosen is consistent with product, promotion, and pricing strategies. In making these decisions, marketing managers must determine what factors will influence the choice of channel and what level of distribution intensity will be appropriate.

FACTORS AFFECTING CHANNEL CHOICE

Managers must answer many questions before choosing a marketing channel. The final choice depends on the analysis of several factors, which often interact. These factors can be grouped as market factors, product factors, and producer factors.

Market Factors

Among the most important market factors affecting the choice of distribution channel are target customer considerations. Specifically, managers should answer the following questions: Who are the potential customers? What do they buy? Where do they buy? When do they buy? How do they buy? Additionally, the choice of channel depends on whether the producer is selling to consumers or to industrial customers. Industrial customers' buying habits are very different from those of consumers. Industrial customers tend to buy in larger quantities and require more customer service. For example, Toyota Industrial Equipment manufactures the leading lift truck used to move materials in and out of warehouses and other industrial facilities. Its business customers buy large numbers of trucks at one time and require additional services such as data tracking on how the lift truck is used. In contrast, consumers usually buy in very small quantities and sometimes do not mind if they get little or no service, such as in a discount store like Wal-Mart or Target.

The geographic location and size of the market are also important to channel selection. As a rule, if the target market is concentrated in one or more specific areas, then direct selling through a sales force is appropriate. When markets are more widely dispersed, intermediaries would be less expensive. The size of the market also influences channel choice. Generally, larger markets require more intermediaries. For instance, Procter & Gamble has to reach millions of consumers with its many brands of household goods. It needs many intermediaries, including wholesalers and retailers.

Product Factors

Products that are more complex, customized, and expensive tend to benefit from shorter and more direct marketing channels. These types of products sell better through a direct sales force. Examples include pharmaceuticals, scientific instruments, airplanes, and mainframe computer systems. On the other hand, the more standardized a product is, the longer its distribution channel can be and the greater the number of intermediaries that can be involved. For example, with the exception of flavor and shape, the formula for chewing gum is about the same from producer to producer. Chewing gum is also very inexpensive. As a result, the distribution channel for gum tends to involve many wholesalers and retailers.

The product's life cycle is also an important factor in choosing a marketing channel. In fact, the choice of channel may change over the life of the product. For example, when photocopiers were first available, they were typically sold by a direct sales force. Now, however, photocopiers can be found in several places, including warehouse clubs, electronics superstores, and mail-order catalogs. As products become more common and less intimidating to potential users, producers tend to look for alternative channels. Gatorade was originally sold to sports teams, gyms, and fitness clubs. As the drink became more popular, mainstream supermarket channels were added, followed by convenience stores and drugstores. Now Gatorade can be found in vending machines and even in some fast-food restaurants.

Another factor is the delicacy of the product. Perishable products like vegetables and milk have a relatively short life span. Fragile products like china and crystal require a minimum amount of handling. Therefore, both require fairly short marketing channels. Online retailers such as eBay facilitate the sale of unusual or difficult-to-find products that benefit from a direct channel.

Producer Factors

Several factors pertaining to the producer itself are important to the selection of a marketing channel. In general, producers with large financial, managerial, and marketing resources are better able to use more direct channels. These producers have the ability to hire and train their own sales force, warehouse their own goods, and extend credit to their customers. For example, variety store Dollar Tree distributes products through retail locations at low prices. To increase cost-efficiency, Dollar Tree has a coast-to-coast logistics network of nine distribution centers to service its almost 3,000 stores.[9] Smaller or weaker firms, on the other hand, must rely on intermediaries to provide these services for them. Compared to producers with only one or two product lines, producers that sell several products in a related area are able to choose channels that are more direct. Sales expenses then can be spread over more products.

Exhibit 13.5

Intensity of Distribution Levels

Intensity Level	Distribution Intensity Objective	Number of Intermediaries in Each Market	Examples
Intensive	Achieve mass-market selling; popular with health and beauty aids and convenience goods that must be available everywhere	Many	Pepsi-Cola, Frito-Lay potato chips, Huggies diapers, Alpo dog food, Crayola crayons
Selective	Work closely with selected intermediaries who meet certain criteria; typically used for shopping goods and some specialty goods	Several	Donna Karan clothing, Hewlett-Packard printers, Burton snowboards, Aveda aromatherapy products
Exclusive	Work with a single intermediary for products that require special resources or positioning; typically used for specialty goods and major industrial equipment	One	BMW cars, Rolex watches

A producer's desire to control pricing, positioning, brand image, and customer support also tends to influence channel selection. For instance, firms that sell products with exclusive brand images, such as designer perfumes and clothing, usually avoid channels in which discount retailers are present. Manufacturers of upscale products, such as Gucci (handbags) and Godiva (chocolates), may sell their wares only in expensive stores in order to maintain an image of exclusivity. Many producers have opted to risk their image, however, and test sales in discount channels. Levi Strauss expanded its distribution to include JCPenney, Sears, and Wal-Mart.

LEVELS OF DISTRIBUTION INTENSITY

Organizations have three options for intensity of distribution: intensive distribution, selective distribution, or exclusive distribution (see Exhibit 13.5).

Intensive Distribution

intensive distribution
A form of distribution aimed at having a product available in every outlet where target customers might want to buy it.

selective distribution
A form of distribution achieved by screening dealers to eliminate all but a few in any single area.

Intensive distribution is a form of distribution aimed at maximum market coverage. The manufacturer tries to have the product available in every outlet where potential customers might want to buy it. If buyers are unwilling to search for a product (as is true of convenience goods and operating supplies), the product must be very accessible to buyers. A low-value product that is purchased frequently may require a lengthy channel. For example, candy, chips, and other snack foods are found in almost every type of retail store imaginable. These foods typically are sold to retailers in small quantities by food or candy wholesalers. The Wrigley Company could not afford to sell its gum directly to every service station, drugstore, supermarket, and discount store. The cost would be too high. Sysco delivers food and related products to restaurants and other food service companies that prepare meals for customers dining out. It is not economically feasible for restaurants to go to individual vendors for each product. Therefore, Sysco serves as an intermediary by delivering all products necessary to fulfill restaurants' needs.[10]

Most manufacturers pursuing an intensive distribution strategy sell to a large percentage of the wholesalers willing to stock their products. Retailers' willingness (or unwillingness) to handle items tends to control the manufacturer's ability to achieve intensive distribution. For example, a retailer already carrying ten brands of gum may show little enthusiasm for one more brand. Intensive distribution is also susceptible to errors when intermediaries who are shipped products are expected to handle them in a pre-specified manner detailed in buyer-seller agreements. For example, executives at Scholastic Books were quite alarmed when some 1,200 of the 12 million copies of the final book in the Harry Potter series, *Harry Potter and the Deathly Hallows*, were mistakenly released a day earlier than the widely publicized release date through an Internet retailing website.[11]

Selective Distribution

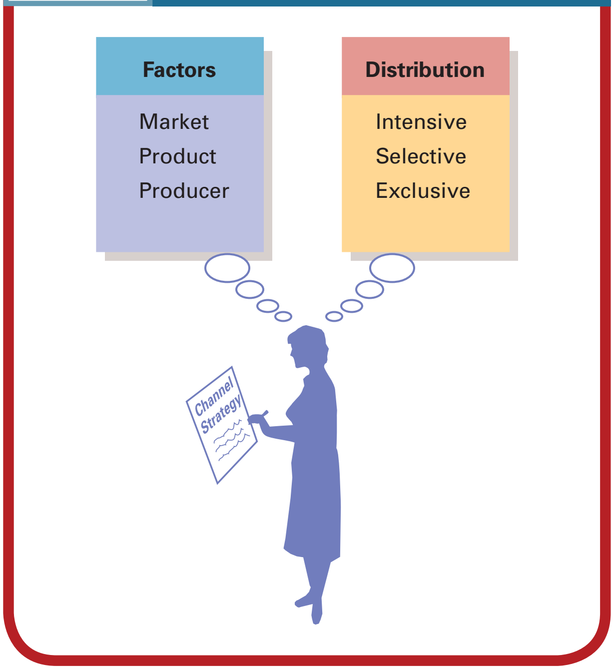
Selective distribution is achieved by screening dealers and retailers to eliminate all but a few in any single area. Because only a few are chosen, the consumer must seek out the product. For example, when Heeling Sports Ltd. launched Heelys, thick-soled sneakers with a wheel embedded in each heel, the company hired a group of 40 teens to perform Heelys exhibitions in targeted malls, skate parks, and college campuses across the country to create demand. Then the company made the decision to avoid large stores like Target and to distribute the shoes only through selected mall retailers and skate and surf shops in order to position the product as "cool and kind of irreverent."[12]

Selective distribution strategies often hinge on a manufacturer's desire to maintain a superior product image so as to be able to charge a premium price. DKNY clothing, for instance, is sold only in select retail outlets, mainly full-price department stores. Likewise, premium pet food brands such as Hill's Pet Nutrition and Ralston-Purina's ProPlan are distributed chiefly through specialty pet food stores and veterinarians, rather than mass retailers like Wal-Mart, so that a premium price can be charged. Manufacturers sometimes expand selective distribution strategies, believing that doing so will enhance revenues without diminishing their product's image. For example, when Procter & Gamble purchased premium pet food brand Iams, it expanded the brand's selective distribution strategy and began selling Iams food in mass retailer Target. Even though the new strategy created channel conflict with breeders and veterinarians who had supported the product, sales increased.[13]

exclusive distribution
A form of distribution that establishes one or a few dealers within a given area.

REVIEW LEARNING OUTCOME

LO4 Discuss the issues that influence channel strategy



Exclusive Distribution

The most restrictive form of market coverage is **exclusive distribution,** which entails only one or a few dealers within a given area. Because buyers may have to search or travel extensively to buy the product, exclusive distribution is usually confined to consumer specialty goods, a few shopping goods, and major industrial equipment. Products such as Rolls-Royce automobiles, Chris-Craft power boats, and Pettibone tower cranes are distributed under exclusive arrangements. Sometimes exclusive territories are granted by new companies (such as franchisors) to obtain market coverage in a particular area. Limited distribution may also serve to project an exclusive image for the product.

Retailers and wholesalers may be unwilling to commit the time and money necessary to promote and service a product unless the manufacturer guarantees them an exclusive territory. This arrangement shields the dealer from direct competition and enables it to be the main beneficiary of the manufacturer's promotion efforts in that geographic area. With exclusive distribution, channels of communication are usually well established because the manufacturer works with a limited number of dealers rather than many accounts.

Exclusive distribution also takes place within a retailer's store rather than a geographic area—for example, when a retailer agrees not to sell a manufacturer's competing brands. Mossimo, traditionally an apparel wholesaler, developed an agreement with Target to design clothing and related items sold exclusively at Target stores. Other exclusive distributors involved in this successful model include Thomas O'Brien domestics, Sonia Kashuk makeup, Isaac Mizrahi domestics and apparel, and Todd Oldham home furnishings for college students.

LO5

Types of Channel Relationships

A marketing channel is more than a set of institutions linked by economic ties. Social relationships play an important role in building unity among channel members. A critical aspect of channel management, therefore, is managing the social relationships among channel members to achieve synergy. Marketing managers should carefully consider the types of relationships they choose to foster between their company and other companies, and in doing so, pay close attention to the benefits and hazards associated with each relationship type.

CHANNEL RELATIONSHIP TYPES

Channel members must create and manage multiple relationships with other members in order to create an efficient environment for exchange. Relationships among channel members range from "loose" to "tight," taking the form of a continuum stretching from single transactions to complex interdependent relationships such as partnerships or alliances. The choice of relationship type is important for channel management because each relationship type carries with it different levels of time, financial, and resource investment. Three basic types of relationships, organized by degree of closeness, are commonly considered: Arm's Length, cooperative, and integrated relationships.

Arm's-Length Relationships

At one end of the relationship continuum are relationships considered by channel members to be temporary or one-time-only. These relationships are often referred to as "Arm's Length" relationships due to the companies' unwillingness or lack of ability to develop a closer type of relationship. In Arm's Length relationships, both parties retain their independence and pursue only their own interests while attempting to benefit from the goods or services provided by the other. This type of relationship is often used when a company has a sudden and/or unique need for a product or service and does not anticipate this need will arise again in the near future. For example, what might happen if Chevrolet were suddenly faced with an unusual situation where Bridgestone, its usual tire producer for the Chevy Tahoe, were unable to provide shipment of tires in reasonable time for a planned production run? One solution might be to engage in a temporary, Arm's Length relationship with an alternate provider such as Michelin, who might be able to supply substitute tires on a temporary basis and thus save Chevrolet the costs associated with delaying the production run.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Arm's Length relationship
A relationship between companies that is loose, characterized by low relational investment and trust, and usually taking the form of a series of discrete transactions with no/low expectation of future interaction or service.

integrated relationship
A relationship between companies that is tightly connected, with linked processes across and between firm boundaries, and high levels of trust and interfirm commitment.

This sort of channel arrangement, however, involves a number of downsides. Because Chevrolet needs the tires on short notice, Michelin might decide to charge a somewhat higher price then usual, and furthermore, because the order placed was a one-time-only order and contained a fixed number of units, it is unlikely that Chevrolet would be able to take advantage of discounts available for customers buying in large quantities. In addition, because the relationship between Chevrolet and Michelin is new, there is no history or friendship to draw on in cases where disagreements or conflicts arise related to the terms of the agreement. In closer relationships, channel members might easily resolve their differences through communication, future promises, or bargaining. But in Arm's Length relationships it is sometimes necessary to resolve Arm's Length disputes through more formal and costly means such as arbitration or lawsuits. For all of these reasons, companies often find it appealing to develop more concrete, long-term relationships with other channel members.

Integrated Relationships

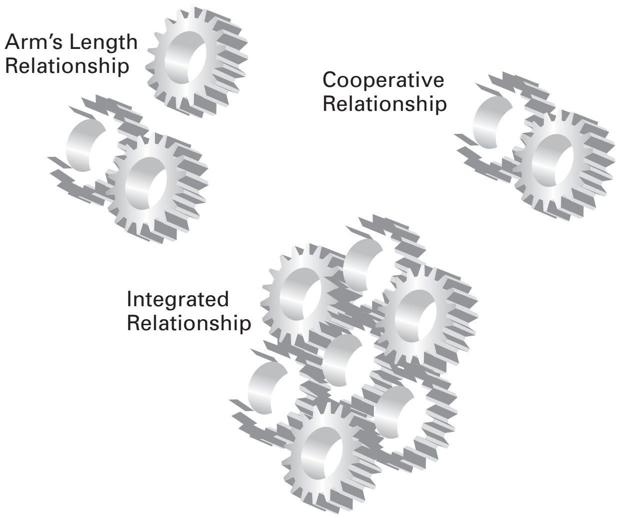
At the opposite end of the relationship continuum from Arm's Length relationships is a situation where one company (vertical integration) or several companies acting as one (a supply chain, see Chapter 14), perform all channel functions. These closely-bonded types of relationships are collectively referred to as integrated relationships. Integrated relationships are characterized by formal arrangements that explicitly define the relationships to the involved channel members. For example, with vertical integration, all of the related channel members are collectively owned by a single legal entity (which may be one of the channel members, or may be a third party), with ownership established through formal legal titles and/or agreements. This sort of relational arrangement has often been employed by McDonald's Corporation, whose subsidiary companies have owned dairy and potato farms and processing plants that grow and process components of the products served by the chain's fast food restaurants. A supply chain, which is discussed in greater depth in Chapter 14, consists of several companies acting together in a highly organized and efficient manner, while employing the same or similar techniques as a single vertically integrated company.

Based on these descriptions, it seems that integrated relationships would be the preferred relationship type in almost all company-to-company channel settings. However, highly integrated relationships also come with some significant costs and/or hazards. For example, the single-owner model is somewhat risky because a large amount of capital assets must be purchased or leased (requiring a potentially huge initial cash outlay), and the failure of any portion of the business may result in not only the economic loss of that portion, but may also reduce the value of the other business units (or render them totally worthless). Because these tradeoffs are sometimes hard to justify, companies often look for a sort of "happy medium" between Arm's Length and integrated relationships that enables them to maximize the advantages of both relationship types while limiting their potential risks.

cooperative relationship
A relationship between companies that takes the form of informal partnership with moderate levels of trust and information sharing as needed to further each company's goals.

REVIEW LEARNING OUTCOME

LO 5 Discuss the different types of channel relationships that exist between channel members, and explain some of the costs and benefits of adopting each relationship type



Cooperative Relationships

Cooperative relationships, which exist between Arm's Length and integrated relationships in terms of their connectedness, take many different forms. Cooperative relationships include non-equity agreements such as franchising and licensing, as well as equity-based joint ventures and strategic alliances (see Chapter 4 for a review). In general, cooperative relationships are administered using some sort of formal contract. This is in contrast to Arm's Length relationships, which are enforced through legal action (or the implied threat thereof), and integrated relationships which rely on informal social enforcement to secure the agreement based on trust, commitment, and loyalty. Cooperative relationships thus tend to be more flexible than integrated relationships, but are also structured with greater detail and depth than Arm's Length relationships. They tend to be used when a company wants less ambiguity in the channel relationship than the Arm's Length relationship can provide, but without the long-term and/or capital investment required to achieve full integration.

LO 6

Managing Channel Relationships

In addition to considering the multiple different types of channel relationships and their costs and benefits, managers must also be aware of the social dimensions that are constantly impacting their relationships. The basic social dimensions of channels are power, control, leadership, conflict, and partnering.

CHANNEL POWER, CONTROL, AND LEADERSHIP

channel power
The capacity of a particular marketing channel member to control or influence the behavior of other channel members.

channel control
A situation that occurs when one marketing channel member intentionally affects another member's behavior.

channel leader (channel captain)
A member of a marketing channel that exercises authority and power over the activities of other channel members.

channel conflict
A clash of goals and methods between distribution channel members.

horizontal conflict
A channel conflict that occurs among channel members on the same level.

Channel power is a channel member's capacity to control or influence the behavior of other channel members. Channel control occurs when one channel member affects another member's behavior. To achieve control, a channel member assumes channel leadership and exercises authority and power. This member is termed the channel leader, or channel captain. In one marketing channel, a manufacturer may be the leader because it controls new-product designs and product availability. In another, a retailer may be the channel leader because it wields power and control over the retail price, inventory levels, and post-sale service.

The exercise of channel power is a routine element of many business activities in which the outcome is often greater control over a company's brands. Apple started its line of retail stores because management was dissatisfied with how distributors were selling the company's computers (i.e., with its lack of control). Macintosh displays were often buried inside other major retail stores, surrounded by personal computers running the more popular Windows operating systems by Microsoft. To regain a position of power in the marketing channel, Apple hired a retail executive to develop a retail strategy, that relied heavily on company-owned stores that reflected Apple's design sensibilities. The new strategy has paid off tremendously: in the first three months of 2006 alone, sales at Apple stores topped $1 billion.[14]

CHANNEL CONFLICT

Inequitable channel relationships often lead to channel conflict, which is a clash of goals and methods among the members of a distribution channel. In a broad context, conflict may not be bad. Often it arises because staid, traditional channel members refuse to keep pace with the times. Removing an outdated intermediary may result in reduced costs for the entire channel. The Internet has forced many intermediaries to offer services such as merchandise tracking and inventory availability online.

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Conflicts among channel members can be due to many different situations and factors. Oftentimes, conflict arises because channel members have conflicting goals. For instance, athletic footwear retailers want to sell as many shoes as possible in order to maximize profits, regardless of whether the shoe is manufactured by Nike, Adidas, or Saucony, but the Nike manufacturer wants a certain sales volume and market share in each market.

Conflict can also arise when channel members fail to fulfill expectations of other channel members—for example, when a franchisee does not follow the rules set down by the franchisor, or when communications channels break down between channel members. As another example, if a manufacturer shortens the period of warranty coverage and fails to inform dealers of this change, conflict may occur when dealers make repairs expecting that they will be reimbursed by the manufacturer. Further, ideological differences and different perceptions of reality can also cause conflict among channel members. For instance, retailers may believe "the customer is always right" and offer a very liberal return policy. Wholesalers and manufacturers may feel that people "try to get something for nothing" or don't follow product instructions carefully. Their differing views of allowable returns will undoubtedly conflict with those of retailers.

Conflict within a channel can be either horizontal or vertical. Horizontal conflict occurs among channel members on the same level, such as two or more different wholesalers or two or more different retailers that handle the same manufacturer's brands. This type of channel conflict is found most often when manufacturers practice dual or multiple distribution strategies. When Apple changed its distribution strategy and began opening its own stores, it angered Apple's traditional retail partners, some of whom ultimately filed lawsuits against the company. The primary allegation was that Apple stores were competing unfairly with them and that Apple favored its own stores when allocating desirable inventory (like iPods). Horizontal conflict can also occur when some channel members feel that other members on the same level are being treated differently by the manufacturer. For example, the American Booksellers Association, a group representing small independent booksellers, filed a lawsuit against bookstore giants Barnes & Noble and Borders, claiming they had violated antitrust laws by using their buying power to demand "illegal and secret" discounts from publishers. These deals, the association contended, put independent booksellers at a serious competitive disadvantage.

vertical conflict
A channel conflict that occurs between different levels in a marketing channel, most typically between the manufacturer and wholesaler or between the manufacturer and retailer.

Many regard horizontal conflict as healthy competition. Much more serious is **vertical conflict,** which occurs between different levels in a marketing channel, most typically between the manufacturer and wholesaler or the manufacturer and retailer. Producer-versus-wholesaler conflict occurs when the producer chooses to bypass the wholesaler and deal directly with the consumer or retailer.

Dual distribution strategies can also cause vertical conflict in the channel. For example, high-end fashion designers traditionally sold their products through luxury retailers such as Neiman Marcus and Saks Fifth Avenue. Interested in increasing sales and gaining additional control over presentation, many designers such as Giorgio Armani, Donna Karan, and Louis Vuitton opened their own boutiques in the same shopping centers anchored by the luxury retailers. As a result, the retailers lost substantial revenues on the designers' items. Similarly, manufacturers experimenting with selling to customers directly over the Internet create conflict with their traditional retailing intermediaries. For example, Walgreens sells about 2 billion photo prints a year, all of which once were printed on Kodak paper using

ETHICS in Marketing

Conflict at Amazon Ends in Divorce

ETHICS

When Toys "R" Us launched its Web site in time for the 1999 holiday shopping season, the company was not ready for the success it was going to have. The site was an instant hit with consumers, but the company had terrible problems filling many orders and was lambasted in the press for weeks after the holiday results were announced. That same year, the world's pioneering e-tailer, Amazon.com, also experienced problems—not with filling orders, but with inventory. Amazon was often out of stock on popular items and overstocked on unpopular ones.

The following year, Amazon and Toys "R" Us brokered what was then considered a landmark deal. Toys "R" Us would sell toys online exclusively through the Amazon.com site. For its part, Amazon would make Toys "R" Us the only toy retailer in its online shopping mall for ten years. After that milestone agreement, Amazon brokered tons of deals with specialty retailers. More than a million companies including Circuit City, Office Depot, Borders, Eddie Bauer, Drugstore.com, Guess?, J&R Music, Ice.com, and Computer World wanted access to the Internet's most reliable order-filling operation. In a single year, the number of online merchants selling through Amazon increased nearly 30 percent.

Then, only two years into its groundbreaking contract with Toys "R" Us, Amazon signed what would become another milestone agreement with Target. The addition of Target angered Amazon's specialty retailers, who saw their exclusive arrangements jeopardized by Target's wide assortment of products. Amazon itself began selling products that ate into its partners' business. For example, Amazon began selling pearl necklaces and diamond earrings, some of the best-selling items at Ice.com, an Amazon partner. Some retailers, like Circuit City, canceled their agreements, saying that they weren't making enough money through Amazon to justify the expense. Toys "R" Us, however, did not go quietly.

Feeling extreme pressure from Wal-Mart and Target off-line, Toys "R" Us sued Amazon for breach of contract (Toys "R" Us still had eight years left in its contract with Amazon). Amazon countersued, arguing that Toys "R" Us was in violation of the agreement because it was not able to supply enough product to Amazon customers. The two companies fought out their disagreement in court until 2006, when a judge formally severed their contract, basically agreeing with Toys "R" Us.

Are multiple distribution channels unethical? Are competition and conflict in the Internet space different than in the physical world of retailing?[16]

Kodak chemicals. When Kodak launched Ofoto.com, a site where customers could upload digital prints to the Internet, view them, and order prints directly from Kodak, Walgreens took exception. It installed 2,300 traditional and digital photo kiosks made by Fuji, Kodak's main competitor. The channel conflict will cost Kodak $500 million a year in sales.[15] This chapter's "Ethics in Marketing" box describes a channel conflict involving Amazon.com.

Producers and retailers may also disagree over the terms of the sale or other aspects of the business relationship. When Procter & Gamble introduced "everyday low pricing" to its retail channel members, a strategy designed to standardize wholesale prices and eliminate most trade promotions, many retailers retaliated. Some cut the variety of P&G sizes they carried or eliminated marginal brands. Others moved P&G brands from prime shelf space to less visible shelves.

Exhibit 13.6

Transaction- versus Partnership-Based Firms

	Transaction-Based	Partnership-Based
Relationships between Manufacturer and Supplier	• Short-term • Adversarial • Independent • Price more important	• Long-term • Cooperative • Dependent • Value-added services more important
Number of Suppliers	Many	Few
Level of Information Sharing	Minimal	High
Investment Required	Minimal	High

SOURCE: David Frederick Ross, *Competing Through Supply Chain Management: Creating Market-Winning Strategies through Supply Chain Partnerships* (New York: Chapman & Hall, 1998), 61. Used with kind permission from Springer Science and Business Media.

CHANNEL PARTNERING

channel partnering (channel cooperation)
The joint effort of all channel members to create a channel that serves customers and creates a competitive advantage.

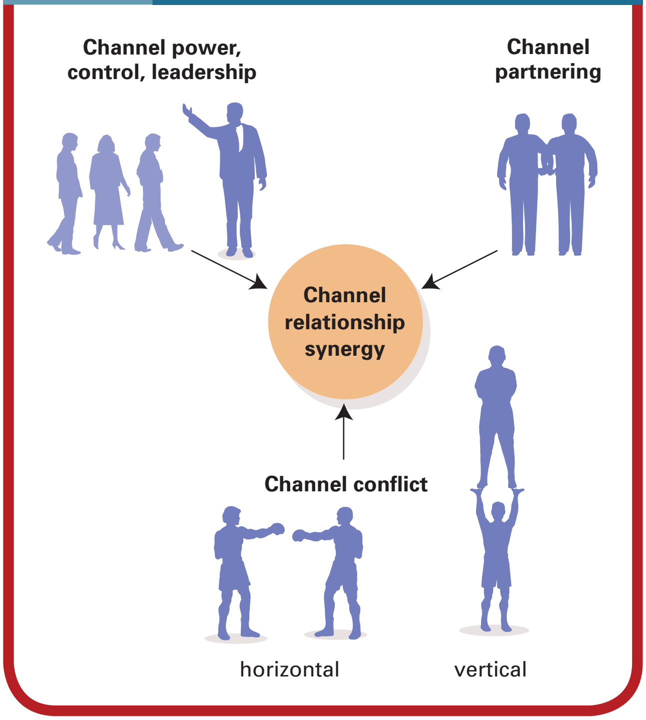
Regardless of the locus of power, channel members rely heavily on one another. Even the most powerful manufacturers depend on dealers to sell their products; even the most powerful retailers require the products provided by suppliers. In sharp contrast to the adversarial relationships of the past between buyers and sellers, contemporary management thought emphasizes the development of close working partnerships among channel members. **Channel partnering,** or **channel cooperation,** is the joint effort of all channel members to create a channel that serves customers and creates a competitive advantage. Channel partnering is vital if each member is to gain something from other members. By cooperating, retailers, wholesalers, manufacturers, and suppliers can speed up inventory replenishment, improve customer service, and reduce the total costs of the marketing channel.

Channel alliances and partnerships help managers create the parallel flow of materials and information required to leverage the channel's intellectual, material, and marketing resources. The rapid growth in channel partnering is due to new enabling technology and the need to lower costs. A comparison between companies that approach the marketplace unilaterally and those that engage in channel cooperation and form partnerships is detailed in Exhibit 13.6.

Collaborating channel partners meet the needs of consumers more effectively by ensuring that the right products are available at the right time and for a lower cost, thus boosting sales and profits. Forced to become more efficient, many companies are turning formerly adversarial relationships into partnerships. For example, Kraft is the largest coffee purchaser in the world. Rather than clash with coffee bean growers, Kraft partners with them to help build customer demand and develop "sustainable" coffee production (growing coffee in a way that reduces the impact on the environment, provides quality ingredients for manufacturers to meet consumer needs, and is more valuable to the farmer).[17]

REVIEW LEARNING OUTCOME

LO6 Explain channel leadership, conflict, and partnering



LO7

Channels and Distribution Decisions for Global Markets

With the spread of free-trade agreements and treaties in recent decades, such as the European Union and the North American Free Trade Agreement (NAFTA), global marketing channels and management of the channels have become increasingly important to U.S. companies that export their products or manufacture abroad.

DEVELOPING GLOBAL MARKETING CHANNELS

Executives should recognize the unique cultural, economic, institutional, and legal aspects of each market before trying to design marketing channels in foreign countries. Manufacturers introducing products in global markets face a tough decision: what type of channel structure to use. Specifically, should the product be marketed directly, mostly by company salespeople, or through independent foreign intermediaries, such as agents and distributors? Using company salespeople generally provides more control and is less risky than using foreign intermediaries. However, setting up a sales force in a foreign country also entails a greater commitment, both financially and organizationally.

Marketers should be aware that channel structures and types abroad may differ from those in the United States. For instance, the more highly developed a nation is economically, the more specialized its channel types. Therefore, a marketer wishing to sell in Germany or Japan will have several channel types to choose from. Conversely, developing countries like India, Ethiopia, and Venezuela have limited channel types available; there are typically few mail-order channels, vending machines, or specialized retailers and wholesalers. Some countries also regulate channel choices. Until 2004, Chinese regulations required foreign retailers to have a local partner. So, when IKEA, the Swedish home furnishings retailer, opened its first two stores in China, it used joint ventures. When the regulations were lifted, however, IKEA opened its first wholly owned store in Guangzhou and then a Beijing store that is almost as big as eight football fields, second in size only to the company's flagship store in Stockholm.[18]

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Developing effective marketing channels in emerging nations is further complicated due to different retail format preferences and differences in the ways locals shop. In many emerging nations, consumers shun large-scale formats popularized in the United States and Western Europe such as super centers and other big-box retailers, in favor of tiny, independently owned street-side retailers that may be no larger than a closet. These small retailers (known at Procter and Gamble as "high frequency shops") provide small-size packages of goods that are intended to fulfill customer needs only for a day or two. Procter and Gamble estimates that over 620,000 such stores exist in Mexico alone, and that 80 percent of emerging nation citizens shop high-frequency stores multiple times per week. New channel strategies are currently being developed by firms like P&G in order to maximize sales and penetration into high frequency shops, including reliance on local sales agents who are paid to ensure popular products are placed as close as possible to the street and/or cash register.[19]

Marketers must also be aware that many countries have "gray" marketing channels in which products are distributed through unauthorized channel intermediaries. It is estimated that sales of counterfeit luxury items like Prada handbags and Big Bertha golf clubs have reached almost $2 billion a year. The new fakes are harder to detect and hit the market almost instantly. For instance, a fake Christian Dior saddlebag was available just weeks after the original arrived on retailers' shelves. Similarly, Chinese companies are producing so many knockoffs of Yamaha, Honda, and Suzuki motorcycles that the Japanese companies are seeing a drop in sales. What's more, many companies are getting so good at design piracy that they are beginning to launch their own new products.

The Internet has also proved to be a way for pirates to circumvent authorized distribution channels, especially in the case of popular prescription drugs. In recent years, the U.S. Customs Service has seized millions of dollars worth of prescription drugs, most of which were purchased from foreign Internet sites. Some were seized because they had not been approved for use in the United States, others because they did not comply with U.S. labeling laws. Most sites offer just a handful of the most popular drugs, such as Viagra. Consumers can get the drugs after obtaining the approval of a doctor affiliated with the site who never sees the patient.

REVIEW LEARNING OUTCOME

LO 7 Discuss channels and distribution decisions in global markets

- Distribute directly or through foreign partners
- Different channel structures than in domestic markets
- Illegitimate "gray" marketing channels
- Legal and infrastructure differences

LO 8

Channels and Distribution Decisions for Services

The fastest-growing part of our economy is the service sector.

Although distribution in the service sector is difficult to visualize, the same skills, techniques, and strategies used to manage inventory can also be used to manage service inventory—for instance, hospital beds, bank accounts, or airline seats. The quality of the planning and execution of distribution can have a major impact on costs and customer satisfaction.

One thing that sets service distribution apart from traditional manufacturing distribution is that, in a service environment, production and consumption are simultaneous. In manufacturing, a production setback can often be remedied by using safety stock or a faster mode of transportation. Such substitution is not possible with a service. The benefits of a service are also relatively intangible—that is, a consumer normally can't see the benefits of a service, such as a doctor's physical exam, but normally can see the benefits provided by a product—for example, cold medicine relieving a stuffy nose.

Because service industries are so customer oriented, customer service is a priority. To manage customer relationships, many service providers, such as insurance carriers, physicians, hair salons, and financial services, use technology to schedule appointments, manage accounts, and disburse information. Service distribution focuses on three main areas:

- *Minimizing wait times:* Minimizing the amount of time customers wait in line to deposit a check, wait for their food at a restaurant, or wait in a doctor's office for an appointment is a key factor in maintaining the quality of service. People tend to overestimate the amount of time they spend waiting in line, researchers report, and unexplained waiting seems longer than explained waits. To reduce anxiety among waiting customers, some restaurants give patrons pagers that allow them to roam around or go to the bar. Banks sometimes install electronic boards displaying stock quotes or sports scores. Car rental companies reward repeat customers by eliminating their waits altogether. Airports have designed comfortable sitting areas with televisions and children's play areas for those waiting to board planes. Some service companies are using sophisticated technology to further ease their customers' waiting time. For example, many hotels and airlines are using electronic check-in kiosks. Travelers can insert their credit cards to check in upon arrival, receive their room key, get directions, print maps to area restaurants and attractions, and print out their hotel bills.

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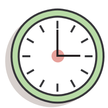
GEICO's early business model—a first in the insurance industry—involved direct marketing to targeted customers without the use of agents. In its early years, GEICO contacted its customers by mail and telephone, but now it offers online service 24 hours a day, seven days a week.

- *Managing service capacity:* For product manufacturers, inventory acts as a buffer, enabling them to provide the product during periods of peak demand without extraordinary efforts. Service firms don't have this luxury. If they don't have the capacity to meet demand, they must either turn down some prospective customers, let service levels slip, or expand capacity. For instance, at tax time a tax preparation firm may have so many customers desiring its services that it has to either turn business away or add temporary offices or preparers. Popular restaurants risk losing business when seating is unavailable or the wait is too long. To manage their capacity, travel Web sites allow users to find last-minute deals to fill up empty airline seats and hotel rooms.
- *Improving service delivery:* Like manufacturers, service firms are now experimenting with different distribution channels for their services. Choosing the right distribution channel can increase the times that services are available (such as using the Internet to disseminate information and services 24/7) or add to customer convenience (like pizza delivery, walk-in medical clinics, or a dry cleaner located in a supermarket). The airline industry has found that using the Internet for ticket sales both reduces distribution costs and raises the level of customer service by making it easier for customers to plan their own travel. Cruise lines, on the other hand, have found that travel agents add value by helping customers sort through the abundance of information and complicated options available when booking a cruise. In the real estate industry, realtors are placing kiosks in local malls that enable consumers to directly access listings.

The Internet is fast becoming an alternative channel for delivering services. Consumers can now purchase plane tickets, plan a vacation cruise, reserve a hotel room, pay bills, purchase mutual funds, and receive electronic newspapers in cyberspace. Insurance giant Allstate, for instance, now sells auto and home insurance directly to consumers in some states through the Internet in addition to its traditional network of agents. The effort reduces costs so that Allstate can stay competitive with rival insurance companies Progressive and Geico that already target customers directly. Similarly, several real estate Web sites are making it easier for customers to shop for a new home on the Web. Traditionally, the only way for customers to gain access to realtors' listings was to work through a real estate agent who would search the listings and then show customers homes that met their requirements. The new companies offer direct access to the listings, enabling customers to review properties for sale on their own and choose which ones they would like to visit.

REVIEW LEARNING OUTCOME

LO8 Identify the special problems and opportunities associated with distribution in service organizations



Minimizing wait times is a key factor in maintaining service quality.

Managing service capability is critical to successful service distribution.

Improving service delivery makes it easier and more convenient for consumers to use the service.

17 < major retailers in the Worldwide Retail Exchange

percentage of purchasing costs saved by using the exchange > **15**

3,000 < Dollar Tree Stores

Dollar Tree distribution centers > **9**

copies of *Harry Potter and the Deathly Hallows* mistakenly released early > **1200**

2 billion < photo prints sold by Walgreens each year

yearly profits Kodak lost to channel conflict with Walgreens > **\$500 billion**

small "high frequency" stores in Mexico > **620,000**

80 < percentages of emerging nation citizens who shop in such stores multiple times each week

Review and Applications

LO 1

Explain what a marketing channel is and why intermediaries are needed. A marketing channel is a business structure of interdependent organizations that reach from the point of product origin to the consumer with the purpose of physically moving products to their final consumption destination, representing "place" or "distribution" in the marketing mix, and encompassing the processes involved in getting the right product to the right place at the right time. Members of a marketing channel create a continuous and seamless system that performs or supports the marketing channel functions. Channel members provide economies to the distribution process in the form of specialization and division of labor; overcoming discrepancies in quantity, assortment, time, and space; and providing contact efficiency.

1.1 Your family runs a specialty ice cream parlor called Scoops. It manufactures its own ice cream in small batches and sells it only in pint-sized containers. After someone not affiliated with the company sent six pints of its ice cream to a popular talk-show host, she proclaimed on her national TV show that it was the best ice cream she had ever eaten. Immediately after the broadcast, orders came flooding in, overwhelming your small-batch production schedule and your limited distribution system. The company's shipping manager thinks she can handle it, but you disagree. List the reasons why you need to restructure your channel of distribution.

LO 2

Define the types of channel intermediaries and describe their functions and activities. The most prominent difference separating intermediaries is whether they take title to the product. Retailers and merchant wholesalers take title, but agents and brokers do not. Retailers are firms that sell mainly to consumers. Merchant wholesalers are organizations that facilitate the movement of products and services from the manufacturer to producers, resellers, governments, institutions, and retailers. Agents and brokers do not take title to the goods and services they market, but they do facilitate the exchange of ownership between sellers and buyers. Channel intermediaries perform three basic types of functions. Transactional functions include contacting and promoting, negotiating, and risk taking. Logistical functions performed by channel members include physical distribution, storing, and sorting functions. Finally, channel members may perform facilitating functions, such as researching and financing.

ONLINE

2.1 What kind of marketing channel functions can be performed over the Internet? Why do you think so?

LO 3

Describe the channel structures for consumer and business products and discuss alternative channel arrangements. Marketing channels for consumer and business products vary in degree of complexity. The simplest consumer-product channel involves direct selling from producers to consumers. Businesses may sell directly to business or government buyers. Marketing channels grow more complex as intermediaries become involved. Consumer-product channel intermediaries include agents, brokers, wholesalers, and retailers. Business-product channel intermediaries include agents, brokers, and industrial distributors. Marketers often use alternative channel arrangements to move their products to the consumer. With dual distribution or multiple distribution, they choose two or more different channels to distribute the same product. Nontraditional channels help differentiate a firm's product from the competitor's or provide a manufacturer with another avenue for sales. Finally, strategic channel alliances are arrangements that use another manufacturer's already established channel.

3.1 Describe the most likely marketing channel structure for each of these consumer products: candy bars, Tupperware products, nonfiction books, new automobiles, farmers' market produce, and stereo equipment. Now, construct alternative channels for these same products.

WRITING

3.2 You have been hired to design an alternative marketing channel for a firm specializing in the manufacturing and marketing of novelties for college student organizations. In a memo to the president of the firm, describe how the channel operates.

WRITING

3.3 Building on question 1.1 determine a new channel structure for Graeter's. Write a proposal to present to your key managers.

LO4

Discuss the issues that influence channel strategy. When determining marketing channel strategy, the channel manager must determine what market, product, and producer factors will influence the choice of channel. The manager must also determine the appropriate level of distribution intensity. Intensive distribution is distribution aimed at maximum market coverage. Selective distribution is achieved by screening dealers to eliminate all but a few in any single area. The most restrictive form of market coverage is exclusive distribution, which entails only one or a few dealers within a given area.

4.1 Decide which distribution intensity level—intensive, selective, or exclusive—is used for each of the following products, and explain why: Piaget watches, Land Rover sport-utility vehicles, M&Ms, special edition Barbie dolls, Crest toothpaste.

TEAM

4.2 Now that you have a basic channel structure for Graeter's (from question 3.3), form a team of three to four students and list the market, product, and producer factors that will affect your final channel structure.

LO5

Describe the different channel relationship types and their unique costs and benefits. Channel relationships can be plotted on a continuum ranging from Arm's Length to integrated, with cooperative relationships somewhere in between. Arm's Length relationships generally consist of unique transactions that are intended to occur once or very infrequently, and are pursued when closer relationships are undesirable or impractical. Though Arm's Length relationships are low risk, they also provide few benefits in terms of favorable conditions for the agreement, and disputes are often resolved in court. Integrated relationships, on the opposite end of the spectrum, are very close relationships that are backed by formal agreements and can result in great efficiency and effectiveness. However, given that integrated relationships tend either to involve high levels of expense (in the case of vertical integration) or require enormous amounts of trust in the partner company (as in the case of supply chains), many companies prefer cooperative relationships in some settings. Cooperative relationships are a hybrid form of relationship that is governed by formal contract, are temporary, and are enforced by the agreement itself.

TEAM

5.1 Working with another student in the class, decide when it would be most advantageous for large companies like Procter & Gamble, IBM, and/or Ford Motor Company to develop integrated relationships with smaller suppliers. Would the same rules for integrated relationship development also apply to customers? Why or why not?

LO6

Explain channel leadership, conflict, power, and partnering. Power, control, leadership, conflict, and partnering are the main social dimensions of marketing channel relationships. Channel power refers to the capacity of one channel member to control or influence other channel members. Channel control occurs when one channel member intentionally affects another member's behavior. Channel leadership is the exercise of authority and power. Channel conflict occurs when there is a clash of goals and methods among the members of a distribution channel. Channel conflict can be either horizontal, between channel members at the same level, or vertical, between channel members at different levels of the channel. Channel partnering is the joint effort of all channel members to create an integrated system that serves customers and creates a competitive advantage. Collaborating channel partners meet the needs of consumers more effectively by ensuring that the right products reach shelves at the right time and at a lower cost, boosting sales and profits.

6.1 Procter & Gamble and Wal-Mart are key partners in a shared channel. P&G is one of Wal-Mart's biggest suppliers, and Wal-Mart provides extremely detailed scanner data about customer purchases of P&G products. Wal-Mart has begun selling its own brand of Sam's

Choice laundry detergent in bright orange bottles alongside P&G's Tide, but for a greatly reduced price. What do you think will be the impact of this new product on what has been a stable channel relationship?

LO7 **Discuss channels and distribution decisions in global markets.** Global marketing channels are becoming more important to U.S. companies seeking growth abroad. Manufacturers introducing products in foreign countries must decide what type of channel structure to use—in particular, whether the product should be marketed through direct channels or through foreign intermediaries. Marketers should be aware that channel structures in foreign markets may be very different from those they are accustomed to in the United States. Global distribution expertise is also emerging as an important skill for channel managers as many countries are removing trade barriers.

ONLINE

7.1 Go to the World Trade Organization's Web site at **http://www.wto.org.** What can you learn at the site about how globalization affects channel management and other aspects of business?

LO8 **Identify the special problems and opportunities associated with distribution in service organizations.** Managers in service industries use the same skills, techniques, and strategies to manage logistics functions as managers in goods-producing industries. The distribution of services focuses on three main areas: minimizing wait times, managing service capacity, and improving service delivery.

WRITING

8.1 Assume that you are the marketing manager of a hospital. Write a report indicating the distribution functions that concern you. Discuss the similarities and dissimilarities of distribution for services and for goods.

Key Terms

agents and brokers	379
Arm's Length relationship	389
channel conflict	391
channel control	391
channel leader (channel captain)	391
channel members	376
channel partnering (channel cooperation)	393
channel power	391
cooperative relationship	390
direct channel	381
discrepancy of assortment	377
discrepancy of quantity	377
dual distribution (multiple distribution)	384
exclusive distribution	388
horizontal conflict	391
integrated relationship	389
intensive distribution	387
logistics	380
marketing channel (channel of distribution)	376
merchant wholesaler	379
retailer	379
selective distribution	387
spatial discrepancy	377
strategic channel alliance	385
temporal discrepancy	377
vertical conflict	392

Exercises

APPLICATION EXERCISE

It may be easy to understand how distribution channels work just from reading, but you may still not appreciate their broad scope. This exercise will help you see for yourself how complex a single distribution channel is. Then, when you think of the number of products and services available on the market at any one time, you will understand how tremendous the national (and international) distribution network actually is.[19]

Activities

1. Create a list of approximately 20 products that you often purchase for personal use and/or that are present in your home.
2. For each of the products you listed, speculate whether the product was routed through the marketing channel using (a) exclusive, (b) selective, or (c) intensive distribution.
3. Now, for each product/distribution strategy combination, speculate as to the product, market, or producer factors that lead to this distribution strategy.

4. Finally, identify any potential alternative distribution channel options through which you might have purchased this product. Would the alternative channel choice have changed the way (location, timing, price) you purchased this good? Why or why not?

ETHICS EXERCISE

Wholesome Snacks, Inc., the maker of a variety of cookies and crackers, has just created a new vitamin-packed cookie. The new cookie has the potential to combat many of the health problems caused by malnutrition in children throughout poverty-stricken areas of the world. To date, however, many of the larger developing markets have resisted opening distribution channels to Wholesome's products. Wholesome realizes that its new cookie could also help open the door for the company to sell its less nutritious products in these markets. Therefore, the company is offering the new cookie at a low cost to government relief programs in exchange for the long-sought distribution channels. The company feels the deal is good for business, but the countries feel it is corporate bullying.

Questions

1. What do you think about Wholesome's idea for opening a new distribution channel?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketingpower.com** and review the code. Then, write a brief paragraph stating what the AMA Statement of Ethics contains that relates to distribution channels in developing nations.

Case Study: Current TV

CURRENT TV PLUGS INTO THE 'NET GENERATION

Ten years ago, the Internet began a revolution that has forever changed the way consumers shop for goods, send and receive mail, find and read news, and acquire and listen to music. A relatively new electronic distribution channel, the Web enables billions of near-instantaneous commercial, consumer, and information exchanges each day. And with the widespread dispersion of increasingly powerful and portable digital technologies, marketers are witnessing a new phenomenon—consumers devoting considerable time to archiving and sharing the personal events of their lives.

Tech-savvy members of Generations X and Y are photographing, recording, cataloging, uploading, blogging, hyperlinking, downloading, and sharing peer-to-peer files at an accelerating pace. Moreover, the independent Web sites where those opinions, files, and reports are located are becoming an increasingly valid means of staying connected with the world. Quite simply, this phenomenon is turning traditional media channels on their collective ear.

Few companies really comprehend that the digital technologies driving homemade reporting and entertainment productions are simultaneously increasing demand for them. One company that understands, and even anticipated, this trend is start-up cable channel Current TV. Cofounded, chaired, and shaped by the vision of former vice president Al Gore, Current predicted the relevance of do-it-yourself (DIY) media some time ago. Gore's objective, as stated on Current TV's Web site, is to democratize the production, distribution, and consumption of television.

Years ago Gore recognized that the proliferation of affordable digital technology would make it possible to create "a powerful new brand of television that doesn't treat audiences as merely viewers, but as collaborators." And those collaborations, fueled by viewer-created content (VCC), are powering the DIY media boom. Shari Anne Brill, vice president and director of programming at the Carat Group, an independent media agency, predicts that "Current will appeal to a much younger-skewing and very unique audience. It opens up tremendous avenues between Internet and television, and it's a very interesting way to reach out to viewers who want to participate in the viewing experience."

Current TV's Web site already hosts a menu of more than 50 "pods" containing program lists chosen for their appeal to independent spirits who have grown disenchanted with the staid format of mainstream television. Recent feature programs on Current TV have included a piece on a man who spends his free time jumping from cliffs and bridges, a first-person perspective on the rescue efforts in the aftermath of Hurricane Katrina, and an in-depth report on a San Francisco rock band produced by a local college student.

Most programs relate to current affairs, but other topics routinely covered include lifestyle themes such as art, fashion, culture, the environment, music, language, relationships, careers, travel, movies, and more. Regardless of subject, all Current TV programming has an intimate and unpretentious feel. Ever mindful of past pitfalls, Current is adamant that it will not devolve into a twenty-first century version of the public access fiascoes that gave VCC a bad name many years ago.

To protect program quality, only one-third of Current's programming is viewer created, but the company doesn't think that will dissuade viewers as long as its professionally produced work has credibility, relevance, and appeal. The viewer-submitted content that is aired is also paid for, though it is repeated quite a bit, and watchers have the ability to vote for shows at Current TV's Web site.

What would enable Current to run more VCC? The answer, in a word, is access. At this time, Current distributes its programming to only 20 million residences in select metropolitan areas via Comcast, DirecTV, and Time Warner. It lacks support from the major cable and satellite companies that, together, feed popular stations to around 80 million homes. Current needs access to viewers in order to appeal to their creative alter egos and fuel the DIY cycle.

In an age when countless business models have seen explosive growth followed by a dramatic collapse, Current's approach and situation look promising. Its concept has recently been validated by MTV's purchase of independent, Web-based VCC site iFilm.com. MTV Networks Music Group president, Brian Graden, says that VCC "is obviously the next wave, and the purchase by Viacom of iFilm is probably the strongest statement that we're very much on to that. The more control you put of everything into the viewers' hands in this sort of multi-platform, on-demand age, that's the only way you're going to win."[21]

Questions

1. Explain Current TV's channel strategy. What factors influence it the most? Why?
2. Describe Current TV's channel arrangement. What role do the intermediaries play? What potential conflicts would you predict for Current?
3. Who are Current's channel partners? What do you think will be needed to sustain those relationships?

Company Clips

SEPHORA—BUSINESS IS BEAUTIFUL

The beauty-retail store Sephora was founded in 1969 in France and since then has become a leader in sales of heath and beauty-aid products. It opened its first store in the United States in 1998 on 5th Avenue in New York City and prides itself on being ahead of the market in skin care trends. Its luxurious environment is the selling point for over 250 brands. On its shelves, Sephora maintains a balance of big brand names with lesser known, up-and-coming brands. Sephora also carries its own private brand that it promotes independently in the store. Each sales representative in a Sephora store is trained to best help customers find the products that best fit their skin types and lifestyles. Watch the video to learn what techniques Sephora uses to keep its shelves stocked and customers happy.

Questions

1. Why is important to customers that Sephora keep detailed information about their inventory? What does Sephora do to insure their numbers are accurate?
2. How does Sephora manage its marketing channel? What information goes into deciding which suppliers become incorporated?

Marketing & You Results

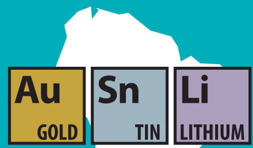
A higher score indicates that you like to be a leader and use authority. Studies have linked authority to vanity, so a high score also suggests a high level of vanity. In particular, you have "achievement view vanity," which is strongly linked to authority. That means that you have very high opinions of your accomplishments and think that others consider you successful as well.

ANATOMY OF A Marketing Channel

Electronics

Channel members facilitate the distribution process by providing specialization and division of labor, overcoming discrepancies, and providing contact efficiency.

Producer



Materials used to make the components of electronic devices come from around the globe, e.g., South America provides tin (solder), lithium (batteries), and gold (a/v cables).

Customers have the option of buying their computer supplies online through a direct channel with the manufacturer.

Distributor

Dual distribution: consumers can buy directly from producers or through a retailer.

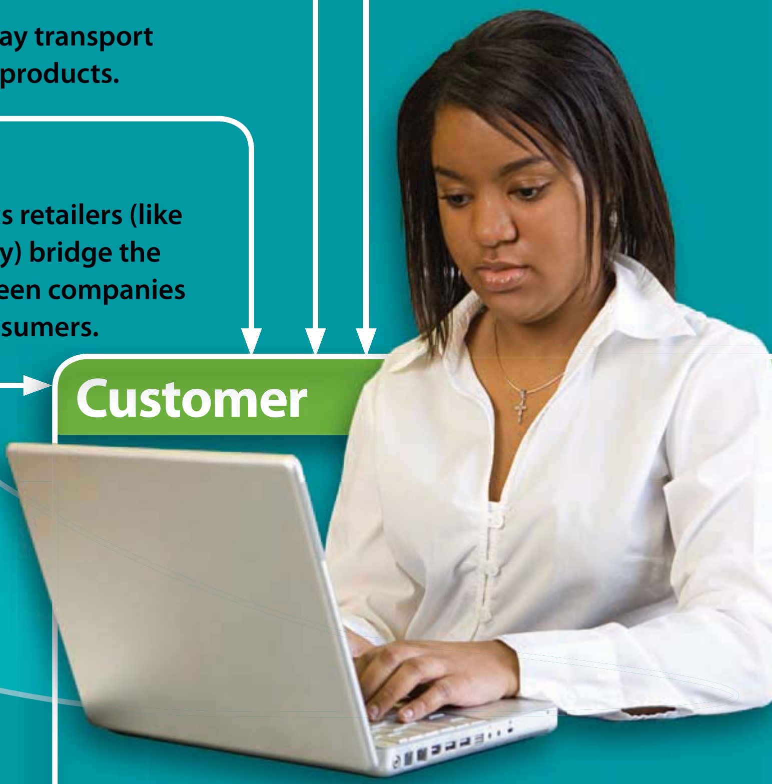
Wholesaler

Wholesalers may transport and distribute products.

Electronics retailers (like Circuit City) bridge the gap between companies and consumers.

Retailer

Customer



CHAPTER 14

Supply Chain Management

Learning Outcomes

LO 1 Define the terms *supply chain, supply chain management,* and *supply chain orientation,* and discuss the benefits of supply chain management

LO 2 Discuss the concept of supply chain integration and explain why each of the six types of integration is important

LO 3 Identify the eight key processes of excellent supply chain management, and discuss how each of these processes impacts the end customer

LO 4 Discuss the key strategic decisions supply chain managers must make when designing their companies' supply chains

LO 5 Describe the logistical components of the supply chain

LO 6 Explain why supply chain performance measurement is necessary and important

LO 7 Discuss new technology and emerging trends in supply chain management

LO 1

Supply Chains and Supply Chain Management

supply chain
The connected chain of all of the business entities, both internal and external to the company, that perform or support the logistics function.

supply chain management
A management system that coordinates and integrates all of the activities performed by supply chain members into a seamless process, from the source to the point of consumption, resulting in enhanced customer and economic value.

In today's sophisticated marketplace, many companies are focusing on their supply chain and turning to supply chain management for competitive advantage. A company's supply chain includes all of the companies involved in all of the upstream and downstream flows of products, services, finances, and information, from initial suppliers (the point of origin) to the ultimate customer (the point of consumption). The goal of supply chain management is to coordinate and integrate the activities performed by supply chain members into a collection of seamless end-to-end processes, ultimately giving supply chain managers "total visibility" of the supply chain both inside and outside the firm. The philosophy behind supply chain management is that by visualizing the entire supply chain, managers can maximize strengths and efficiencies at each level of the process to create a highly competitive, customer-driven supply system that is able to respond immediately to changes in supply and demand. Companies that have a supply chain orientation are those that recognize and embrace this philosophy, and therefore see the implications of managing the flows of products, services, etc. across their direct and indirect suppliers and customers.

An important element of supply chain management is that it is completely customer driven. During the era of mass-production (c.1865–1980), manufacturers produced standardized products that were "pushed" down through the supply channel to the consumer. In contrast, products in today's marketplace are being driven by customers, who expect to receive product configurations and services matched to their unique needs. For example, Dell only builds computers according to its customers' precise specifications, such as the amount of RAM memory; type of monitor, modem, or CD drive; and amount of hard disk space. Similarly, car companies offer customers the option to customize even economy-priced cars. For about $20,000, customers can order a Ford Mustang with a V-6 engine, a six-disc CD changer, MP3 player, and eight speakers. The focus is on pulling products into the marketplace and partnering with members of the supply chain to enhance customer value. Customizing an automobile is now possible because of new supply chain relationships between the automobile manufacturers and the after-market auto-parts industry.[1]

This reversal of the flow of demand from a "push" to a "pull" system has resulted in a radical reformulation of market expectations as well as traditional marketing, production, and distribution functions. Through the coordinated partnership of suppliers, manufacturers, wholesalers, and retailers working together along the entire supply chain, supply chain management allows companies to respond with the unique product configuration and mix of services demanded by the customer. Today, supply chain management plays a dual role: first, as

Marketing & You

Think about your current (or most recent) job. Enter the number that most closely corresponds with your opinion on the lines provided, using the scale below.

1	2	3	4	5
Strongly disagree				Strongly agree

— I feel strongly about improving the quality of my organization's services.

— I enjoy discussing quality-related issues with people in my organization.

— I gain a sense of personal accomplishment in providing quality services to my customers.

— I am willing to put in a great deal of effort beyond what is normally expected in order to help my organization deliver high quality services to our customers.

— The way I feel about quality is very similar to the way my organization feels about quality.

— I really care about the quality of my organization's services.

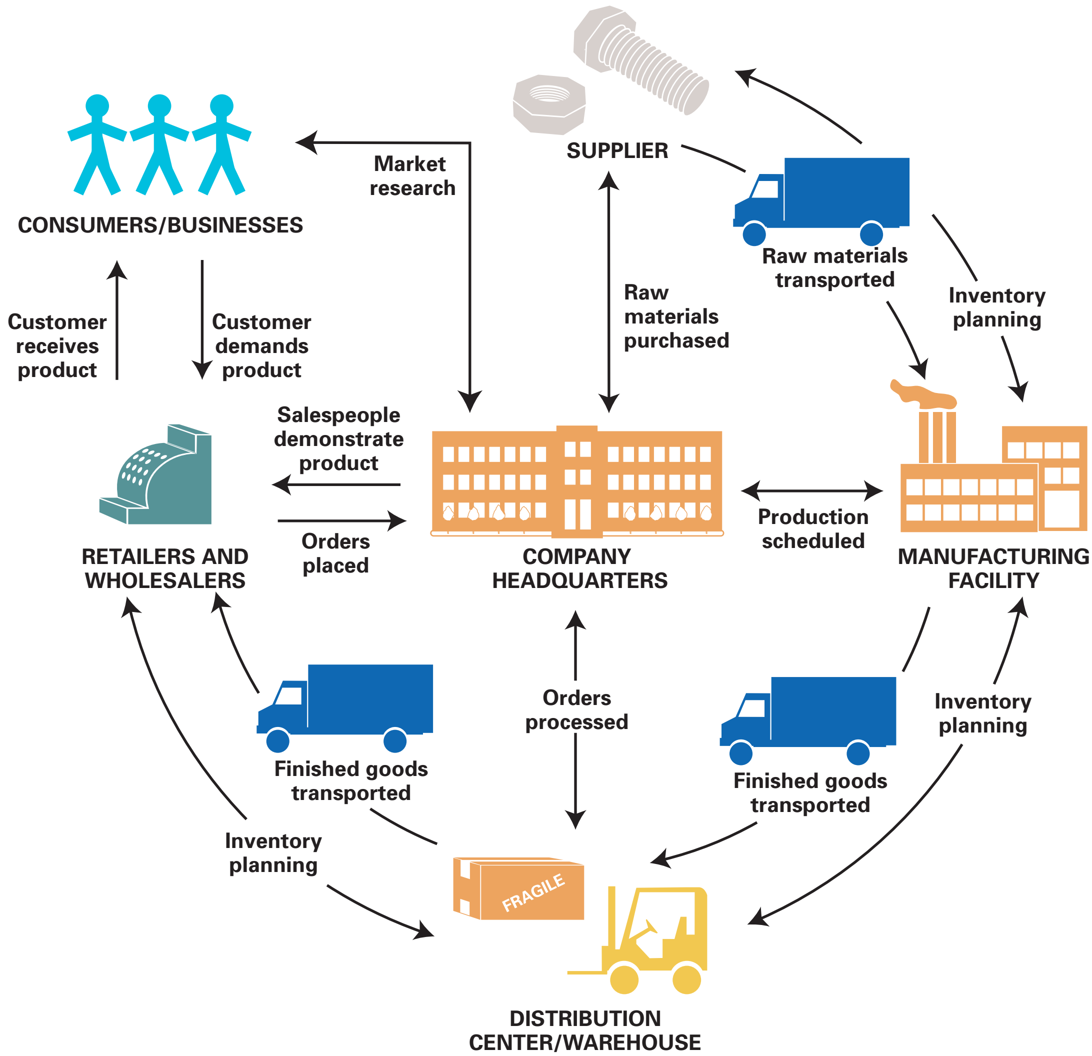
Now, total your score. Find out what it means after you read the chapter.

a *communicator* of customer demand that extends from the point of sale all the way back to the supplier, and second, as a *physical flow process* that engineers the timely and cost-effective movement of goods through the entire source-to-consumer supply pipeline. Boeing realized the importance of these supply chain processes when it struggled to get enough titanium fasteners to assemble the new 787 Dreamliner from its supplier, Alcoa, in time to launch its widely publicized new luxury airliner.[2] Better communication with Alcoa and its titanium ore suppliers, combined with better process flow synchronization, could have reduced the stress Boeing executives felt as they scrambled to find enough fasteners to meet the publicized launch date.

Supply chain managers are responsible for making strategic decisions, such as coordinating the sourcing and procurement of raw materials, scheduling production, processing orders, managing inventory, transporting and storing supplies and finished goods, dealing with returns, and coordinating customer service activities. Supply chain managers are also responsible for the management of information that flows through the supply chain. Coordinating the relationships between the company and its external partners, such as vendors, carriers, and third-party companies, is also a critical function of supply chain management. Because supply chain managers play such a major role in both cost control and customer satisfaction, they are more valuable than ever. In fact, demand for supply chain managers has increased substantially in recent years. According to the *Council of Supply Chain Management Professionals*, the supply chain career field accounts for over 9.5 percent of the US gross domestic product, with thousands of new, high-paying positions becoming available yearly.

Exhibit 14.1

A Typical Supply Chain Management Process

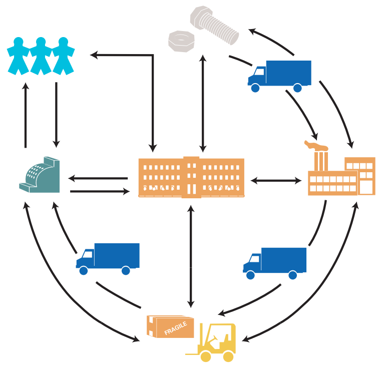


In summary, supply chain managers are responsible for directing raw materials and parts to the production department and the finished or semi-finished product through warehouses and eventually to the intermediary or end user. Above all, supply chain management begins and ends with the customer. Instead of forcing a product into the market that may or may not sell quickly, supply chain managers react to actual customer demand. By doing so, they minimize the flow of raw materials, finished product, and packaging materials at every point in the supply chain, resulting in lower costs and increased customer value. Exhibit 14.1 depicts a typical supply chain model that managers attempt to optimize for firm and customer benefit.

REVIEW LEARNING OUTCOME

LO 1 Define the terms *supply chain, supply chain management,* and *supply chain orientation* and discuss the benefits of supply chain management

Well-managed supply chains . . .



lead to . . .

- ✓ reduced costs
- ✓ increased flexibility
- ✓ improved customer service
- ✓ greater revenue

BENEFITS OF SUPPLY CHAIN MANAGEMENT

Supply chain management is a key means of differentiation for a firm and a critical component in marketing and corporate strategy. Supply chain oriented companies commonly report lower inventory, transportation, warehousing, and packaging costs; greater supply chain flexibility; improved customer service; and higher revenues. Research has shown a clear relationship between supply chain performance and profitability. Specific benefits from effective implementation of supply chain procedures include an almost 20 percent increase in cash flow, a more than 50 percent increase in flexibility of supply chain activities, and a reduction of 5 to 10 percent in supply chain costs, among other potential benefits.[3]

LO 2 Supply Chain Integration

A key principle of supply chain management is that multiple firms work together to perform tasks as a single, unified system, rather than as several individual companies acting in isolation. Companies in a world-class supply chain combine their resources, capabilities, and innovations such that they are used for the best interest of the entire chain as a whole, with the goal being that overall performance of the supply chain will be greater than the sum of its parts. As firms become increasingly supply chain oriented, they develop management practices that are consistent with this systems approach.

Management practices that are reflective of a highly coordinated effort between supply chain partners are said to be "integrated." In other words, supply chain integration occurs when multiple firms in a supply chain coordinate their activities and processes so that they are seamlessly linked to one another in an effort to satisfy the customer. In a world-class supply chain, the customer may not know where the business activities of one firm or business unit end, and where those of another begin—all of the participating firms and business units appear to be reading from the same script.

system approach
A key principle of supply chain management—that multiple firms work together to perform tasks as a single, unified system, rather than as several individual companies acting in isolation.

supply chain integration
When multiple firms in a supply chain coordinate their activities and processes so that they are seamlessly linked to one another in an effort to satisfy the customer.

relationship integration
The ability of two or more companies to develop social connections that serve to guide their interactions when working together.

role specificity
When each firm in a supply chain has clarity in terms of knowing which firm is the leader, which firms are the followers, and which responsibilities are assigned to each firm.

In the practice of world-class supply chain management, six types of integration are sought by firms interested in providing top-level service to customers.[4] In terms of firm-to-firm social interactions, relationship integration provides important benefits. For the purposes of operational planning and control, *measurement integration* and *technology and planning integration* have been shown to be important determinants of company and overall supply chain success. When executing daily operations, three other types of integration are worthy of consideration: *material and service supplier integration, internal operations integration,* and *customer integration*. Each of these six types of integration are described in greater detail in the following sections. Firms' success in achieving each of these types of integration is very important. Highly integrated supply chains (those that are successful in achieving many or all of these types of integration) have been shown to be better at satisfying customers, managing costs, delivering high-quality products, enhancing productivity, and utilizing company or business unit assets, all of which translate into greater profitability for the firms and their partners working together in the supply chain.

RELATIONSHIP INTEGRATION

Companies that are integrated with each other are connected in a number of different ways; some very tangible, and some less tangible. Tangible connections might include phone lines, storage in common databases, or having common procedures or formal processes. However, some of the most important ways of integrating supply chain partners are more intangible. These linkages often take the form of social relationships between the members of coordinating or collaborating companies. Relationship integration is the ability of two or more companies to develop social connections that serve to guide their interactions when working together. More specifically, relationship integration is the capability to develop and maintain a shared mental framework across companies that describes how they will depend on one another when working together. This includes the ways in which they will collaborate on activities or projects so that the customer gains the maximum amount of total value possible from the supply chain.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Relationally integrated supply chains have a set of rules, policies, and/or procedures that dictate how firms will work together, and specify how conflicts among supply chain partners will be resolved.

When multiple firms in a supply chain have achieved high relationship integration, they have developed certain social characteristics that allow the entire supply chain to perform at a higher level than would be possible for any of the partners operating alone. For example, relationally integrated supply chains typically have high role specificity; that is, each firm in the supply chain has clarity in terms of knowing which firm is the leader, which firms are the followers, and which responsibilities are assigned to each firm. Relationally integrated supply chains also tend to be managed by formal or informal social guidelines—a set of rules, policies, and/or procedures that dictate how firms will work together and specify how conflicts among supply chain partners will be resolved. In addition, relationally integrated supply chains tend to be open to information sharing across firm/business unit boundaries, so that everyone involved in the supply chain can clearly see the problems and opportunities that arise while firm-to-firm collaboration is taking place. Finally, the supply chains that have developed the highest degrees of relational integration also tend to practice equitable risk/reward sharing. The firms within such supply chains are openly willing to accept fair amounts of gain and loss when things go better, or significantly worse, than expected.

measurement integration
The performance assessment of the supply chain as a whole that also holds each individual firm or business unit accountable for meeting its own goals.

activity-based costing (ABC)
An accounting method used in measurement integration to assess the costs associated with each supply chain activity.

technology and planning integration
The creation and maintenance of information technology systems that connect managers across and through the firms in the supply chain.

MEASUREMENT INTEGRATION

At a somewhat more tangible level, firms in integrated supply chains generally come to some consensus as to how each firm in the supply chain, and the whole of the supply chain itself, will measure its failures and successes. Measurement integration reflects the idea that performance assessments should be transparent and measurable across the borders of different business units and firms, and also assess the performance of the supply chain as a whole while holding each individual firm or business unit accountable for meeting its own goals. Though achieving measurement integration may sound simple, it actually represents a very difficult set of tasks. Supply chain members, though connected, typically come from a variety of industries and play very different roles in the supply chain; standards for performance and measures of performance can vary widely from industry to industry.

Several areas of capability have been identified that are helpful in generating measurement integration across the supply chain. First, managers in all firms and business units must conduct functional assessments—in other words, each department in each business must have its own set of operational success measures, and if possible, similar departments should use the same performance metrics from business to business. Second, the firms in the supply chain should agree on and commit to principles of activity-based costing (ABC). ABC focuses on accounting for costs associated with each enacted activity, regardless of who in the firm or supply chain performs it. Through the use of ABC, costs can be accurately assigned to products, services, departments, or specific customers. Once ABC and functional assessment procedures are in place, all of the firms in the supply chain must then agree to valuate decisions based on a total cost perspective—the idea that all costs for a decision across the entire supply chain should be considered when making a commitment to a decision or project. Finally, there must be a widely agreed-upon set of supply chain metrics that are to be used as standards, both in terms of operational success (for instance, the number of late shipments in a given time period that are considered to be "acceptable," or the number of damaged cartons that can be shipped without paying a penalty), as well as financial success (for instance, what level of profitability or amount of cash flow should be expected). When supply chains achieve high measurement integration, managers have greater ability to act on information flowing through firms and across the supply chain and can take better advantage of market opportunities or detect threats before they become problematic.

TECHNOLOGY AND PLANNING INTEGRATION

World-class supply chain management depends on thorough, accurate, and timely information acquisition and usage. If supply chain managers don't know the facts about their business environment, they cannot make good decisions about what to do now or in the future. By achieving technology and planning integration across their supply chains, firms can gain the information needed to execute short- and long-term planning, and thereby make better operational decisions. Technology and planning integration refers to the creation and maintenance of information technology systems that connect managers across and through the firms in the supply chain; It requires information hardware and software systems that can exchange information when needed between customers, suppliers, and internal operational areas of each of the supply chain partners.

Several firm-level and supply chain-level capabilities must be developed in order for technology and planning integration to become a reality. First, firms in the supply chain must become experts at information management—there must be seamless information flows related to customers, inventory levels, shipments, etc. across all relevant supply chain members. Packets of information must be available in real-time, and accessible whenever and wherever needed in order to enhance the customer's experience. Additionally, supply chain managers within firms and business units should possess strong internal communications capability, meaning that information does not get caught in departmental silos, but rather, is spread where needed throughout the company. Similarly, managers must be connected to managers of other firms via some sort of external connectivity, such that they can share and discuss needed information and view it in a timely, responsive, and usable format. By moving toward the development of these types of capabilities, managers have greater access to valuable information when and where they need it and can make important decisions that benefit the firm and the supply chain in time to take advantage of new opportunities or to stave off competitive threats.

MATERIAL AND SERVICE SUPPLIER INTEGRATION

The popularization of demand-based *pull systems* over the past several years has prompted firms to rethink the processes they use when serving customers. To operate pull systems efficiently, it is necessary to acquire materials used in production both cheaply and effectively. As a result, another type of integration—material and service supplier integration (sometimes called simply supplier integration)—has become a key supply chain focus. Supplier integration, when first considered, sounds simple: firms should link seamlessly to those outsiders that provide goods and services to them, so that they can streamline work processes and thereby provide smooth, high-quality customer experiences. However, as with the other types of integration already discussed, integrating with suppliers is more complex than it would initially seem.

material and service supplier integration
The strategic alignment between a firm and their supply chain materials and services providers that enables the firm to streamline work processes and provide smooth, high-quality customer experiences.

internal operations integration
Links internally performed work into a seamless process that stretches across departmental and/or functional boundaries, with the goal of satisfying customer requirements.

Firms that have developed high levels of supplier integration typically exhibit significant strategic alignment between themselves and their materials and services providers. This means that both sides have a common vision of the total value creation process and are each willing to share the responsibility for satisfying customer requirements. Because this step is so important, firms must choose their suppliers very carefully, paying close attention to each supplier's strategic goals and operational capabilities. Supplier integration also requires that the supply chain partners interact in ways that minimize waste and redundancy, with such interactions extending upward though the supply chain to the supplier's suppliers, and so on. Finally, for true supplier integration to occur, both firms must have a stake in the outcomes of their interactions. As with relationship integration, risk and reward sharing between the firm and its suppliers should be built into any agreements or contracts so that both firms feel committed to serving the end customer over the long term.

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According to a recent article in *Manufacturing Business Technology*, after Volvo Construction Equipment redesigned its supply chain with software that connected all its suppliers to a single order interface, their over-the-counter availability of parts increased from 60 percent to 95 percent.

INTERNAL OPERATIONS INTEGRATION

To provide a seamless and satisfying customer experience, everyone working within the firm must be "on the same page" in terms of daily operations. A fundamental challenge being experienced by most businesses is the need for integrating various departments within the firm, such as marketing, research, sales, and logistics, all of which help in creating and delivering the value-added customer offering. If all of the organizational areas do not work well together, the customer might undergo an experience where they receive different answers to the same question depending on whom they call, or they might be delivered a product or service that is not exactly what was ordered or needed. Process excellence within the firm requires that internal operations be fully integrated. Internal operations integration is the result of capabilities development toward the goal of linking internally performed work into a seamless process that stretches across departmental and/or functional boundaries, with the goal of satisfying customer requirements.

Five distinct groups of activities are related closely to internal operations integration success. First, the firm must become cross-functionally unified. This means that all activities that are worked on by more than one functional department or area should be viewed as a single activity rather than multiple activities worked on by different groups, and that multi-group synergy should be cultivated where applicable. This task is often (but not necessarily) accomplished though the use of cross-functional work teams, whose membership represents each of the relevant departments where the work flow operates. Next, the firm should seek to standardize operations and work processes across workgroups to reduce uncertainty about the ways and methods through which tasks are completed. Third, once cross-functionality and standardization are established, all work processes should be simplified as much as possible so that the best, quickest, and most efficient practices adopted by any of the departments are adopted (where appropriate) by all departments. Based on these processes, process standards should then be developed that provide internal benchmarks for performance. Finally, once common procedures are developed, measured, and evaluated, the overall logistical network of the firm should be reconfigured so that the physical assets owned by the firm can be used in the most efficient order and manner. However, this final step toward internal operations integration should only take place after careful consideration and consultation with work design engineers or other experts, as this step means permanent structural changes to capital assets and can therefore be very costly.

benchmarks
The standards set by measuring the best, quickest, and most efficient work practices.

customer integration
A competency that enables firms to offer long-lasting, distinctive, value-added offerings to those customers who represent the greatest value to the firm or supply chain.

ABC segmentation
The supply-chain process whereby customers are placed into groups A, B, and C according to their overall long-term value to the firm and to the extent to which the firm can serve their desires.

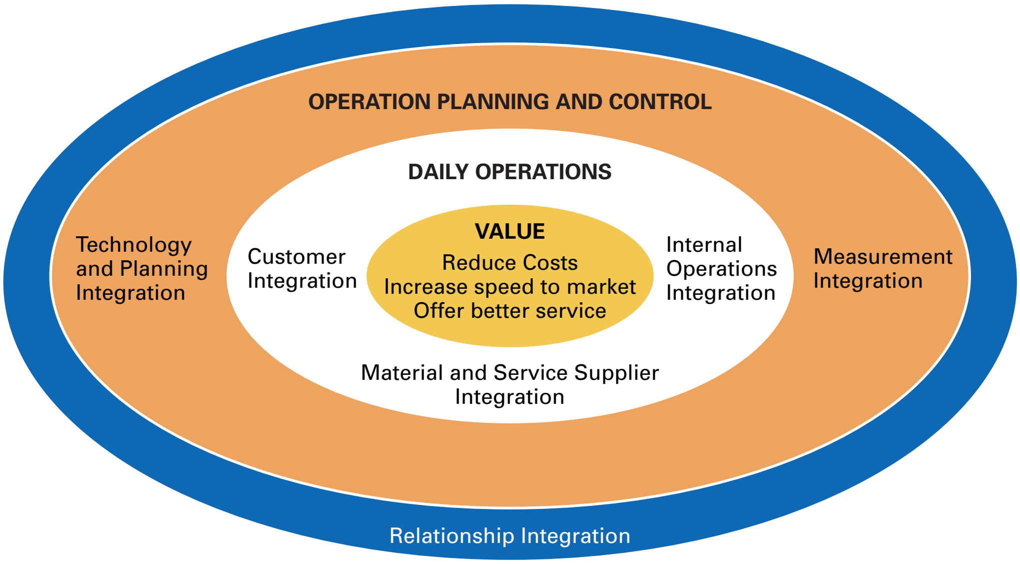
CUSTOMER INTEGRATION

All of the previously discussed forms of integration are critical to the success of the supply chain. However, none may be more important than supply chain firms' integration with end users of the products and services that the supply chain provides. Supply chain success depends on the ability of all of the involved firms and business units to work together and create value for the customer. Furthermore, to be truly successful, the firms in the supply chain must do so at cost levels that allow everyone in the chain to make a profit. The best way to deliver value under profitability constraints is through customer integration. Customer integration is a competency that enables firms to offer long-lasting, distinctive, value-added offerings to those customers who represent the greatest value to the firm or supply chain. Customer integration requires that supply chain firms know a lot about both themselves and their potential customer base. Highly customer integrated firms assess their own capabilities and then match them to customers whose desires they can meet and who offer large enough sales potential for the linkage to be profitable over the long-term.

As was the case with several other bases of integration, customer integration implies that a number of drivers be present for overall success. First, firms must understand that not all customers are alike, and they should use market segmentation to discover which of the pool of potential customers would be best satisfied by the core competencies of the supply chain. This segmentation should be based upon both the current needs expressed by the customer, and any potential future needs that have yet to be fully articulated. Once the customer pool is segmented according to the extent to which the supply chain can serve them, firms should select customer groups for whom to provide the highest levels of service. This process is often referred to as ABC segmentation—customers are placed into groups A, B, and C according to their overall long-term value to the firm and to the extent to which the firm can serve their desires. Based on ABC segmentation, levels of customer integration are established. For better customers (the A's, for example), high levels of responsiveness, customized offerings, and offering flexibility (in terms of details, finishing, delivery times, etc.) are established. For the next tier of customers, often the B's, standard offerings are made available. At the third tier, usually the C-level customers, minimal direct contact is used, with telemarketing or direct mail being the primary method of contact, and little to no extra value services offered. Thus, customer integration provides stronger, more personal and "connected" experiences for the best customers, while minimizing operational flexibility for customers that are determined to be less valuable.

REVIEW LEARNING OUTCOME

LO 2 Discuss the concept of supply chain integration and explain why each of the six types of integration is important



LO 3 The Key Processes of Supply Chain Management

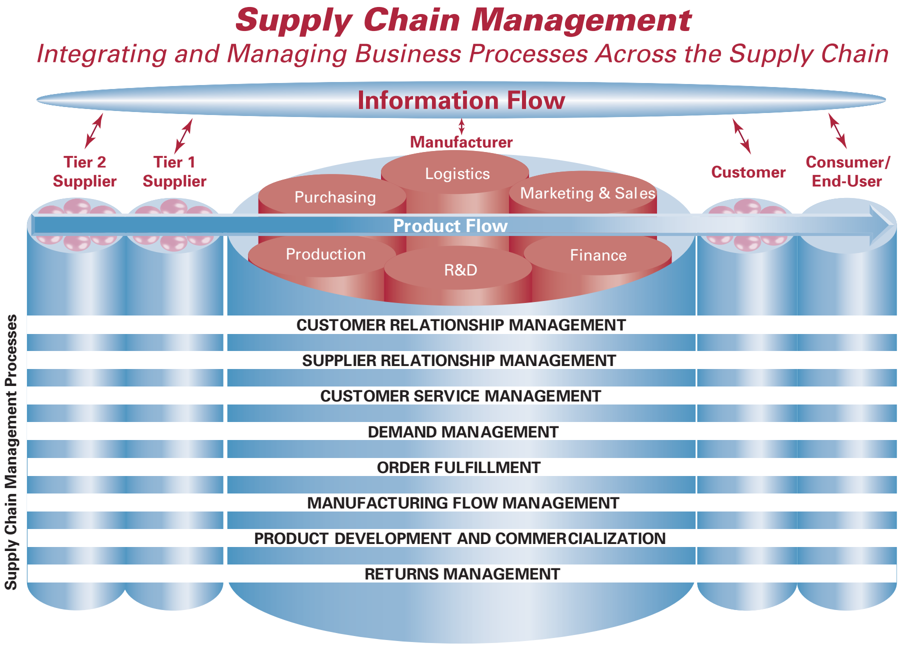
business process Bundles of interconnected activities that stretch across firms in the supply chain.

When firms practice good supply chain management, their functional departments or areas, such as marketing, research and development, and/or production, are integrated both within and across the linked firms. Integration, then, is "how" excellent supply chain management works. The business processes on which the linked firms work together represent the "what" of supply chain management—they are the objects of focus on which firms, departments, areas, and people work together when seeking to reduce supply chain costs or generate additional revenues. Business processes are composed of bundles of interconnected activities that stretch across firms in the supply chain; they represent key areas that some or all of the involved firms are constantly working on in order to reduce costs and/or generate revenues for everyone throughout supply chain management.

There are eight critical business processes on which supply chain managers must focus[5]. These are displayed as the horizontal bars in Exhibit 14.2. As can be seen, some processes extend end-to-end in the supply chain; they are touched or affected by all of the supply chain's firms. Others may be the focus of only 2-3 of the involved companies. Nonetheless, most supply chains operate each of the eight key business processes within some firms and/or business units.

Exhibit 14.2

Supply Chain Management Processes Across the Supply Chain



Source: Douglas M. Lambert, Editor, *Supply Chain Management: Processes, Partnerships, Performance*, Third Edition, Sarasota, FL: Supply Chain Management Institute, 2008, p. 3. Copyright 2008, Supply Chain Management Institute. For more information see: www.scm-institute.org

CUSTOMER RELATIONSHIP MANAGEMENT

customer relationship management process The prioritization of a firm's marketing focus on different customer groups according to each group's long-term value to the company or supply chain; designed to identify and build relationships with good customers.

The customer relationship management process (discussed further in Chapter 21) allows companies to prioritize their marketing focus on different customer groups according to each group's long-term value to the company or supply chain. As noted earlier, some customers are more valuable than others due to their having greater purchasing potential or lower cost-to-serve than others. Once higher-value customers are identified, firms should focus on providing customized products and better service to this group than to others. Activities that are included in the customer relationship management process might include customer differentiation and scoring, identification of new opportunities with valued accounts, and developing customized product and service agreements for upper-tier customer groups, among others. Thus, the customer relationship management process includes both segmentation of customers by value and the generation of customer loyalty for the most attractive segments—key activities that are enabled through customer integration. This process provides a set of comprehensive principles for the initiation and maintenance of customer relationships and is often carried out with the assistance of specialized CRM (Customer Relationship Management) computer software.

Companies that emphasize the customer relationship management process throughout their supply chains are able to deliver best-in-class customer experiences and generate enormous customer loyalty. For example, at 1-800-Flowers.com, data about customer tastes, preferences, and/or order history is collected at all customer contact points. The company then uses this data to better anticipate customer needs and adapt to new trends in the ways, times, and channels through which customers buy flowers. It also reduces the time required to process orders, evaluate a customer's likelihood of buying a new item based on previous orders, assess customer credit worthiness, and customize promotions so that customers are more likely to respond positively.[6] All of these factors allow 1-800-Flowers.com to invest its resources more efficiently and to make better decisions in response to changes in the flower marketplace.

CUSTOMER SERVICE MANAGEMENT

customer service management process
A multi-company, unified response system to the customer whenever complaints, concerns, questions, or comments are voiced; designed to ensure that customer relationships remain strong.

demand management process
The alignment of supply and demand throughout the supply chain to anticipate customer requirements at each level and create demand-related plans of action prior to actual customer purchasing behavior.

Whereas the customer relationship management process is designed to identify and build relationships with good customers, the customer service management process is designed to ensure that those customer relationships remain strong. The customer service management process presents a multi-company, unified response system to the customer whenever complaints, concerns, questions, or comments are voiced. It includes activities such as taking customer calls or requests for information, capturing their order amendments or questions, developing response procedures, amending orders, answering questions, aiding in installation, measuring customer satisfaction with the service encounter, and checking warranty status, among many others. When the process is well-executed, it can have a strong positive impact on revenues, often as a result of quick positive response to negative customer feedback, and sometimes even in the form of additional sales gained through the additional customer contact. Customers expect service from the moment a product is purchased until it is disposed of, and the customer service management process allows for touch points between the buyer and seller throughout this life cycle.

Customer service management processes are increasingly being enhanced through the use of customer care software applications. For example, customer service agents at companies such as Southwest Airlines, Microsoft, and America Online are able to quickly access customers' purchasing, billing, and ordering records on their computer desktops and can use this information to provide a more pleasant interactive experience when customers call to ask questions or complain. Other companies, such as Dell, offer online chat sessions and self-assistance groups on their corporate Web sites so that customers can begin to help themselves prior to (or instead of) making direct contact with the company. Top-level customer service programs also tend to take a very proactive approach to ensuring that customers are satisfied. For example, a person buying a new Lexus automobile can expect to be frequently contacted during their first two years of ownership by associates charged with making sure that the customer's car is meeting their expectations. The associates are empowered to take a wide variety of steps to ensure that customers are satisfied, including offering free service calls, performing customer-location car pickup (including a complimentary loaner car) when adjustments need to be made to automobile settings, and providing free car washes for customers who need unexpected service early in the life of the car.

DEMAND MANAGEMENT

The demand management process seeks to align supply and demand throughout the supply chain by anticipating customer requirements at each level and creating demand-related plans of action prior to actual customer purchasing behavior. At the same time, demand management seeks to minimize the costs of serving multiple types of customers who have variable wants and needs. In other words, the demand management process allows companies in the supply chain to satisfy customers in the most efficient and effective ways possible. The activities that allow the demand management process to work include customer data collection, forecasting of future demand, synchronization of supply and demand by comparing production capacity to forecasts (known as operations planning), and the development of activities that serve to "smooth out" demand, such as authoring short-term promotions, changing salesperson incentives, and revising customer credit terms to reduce default rates. All these activities help to bring available inventory into alignment with customer desires. Though it is very difficult to predict exactly what items and quantities customers will buy prior to purchase, demand management can ease the pressure on the production process and allow companies to satisfy most of their customers through greater flexibility in manufacturing, marketing, and sales programs.

Good demand management can increase both sales and customer satisfaction, and at the same time, it can reduce the overall cost of serving the firm or supply chain's customer base. The positive effects of good demand management can be observed at IKEA. Until 2003, IKEA had traditionally focused primarily on manufacturing and merchandising to generate sales—they used a push system, producing what was likely to sell, and then selling and promoting what was produced—and managed their base of over 1,600 suppliers manually. When unusually large orders were placed for an item, IKEA's distribution centers were emptied, and when fewer orders than expected came, the DC's sat full of unwanted product. After implementing a demand management program developed for them by logistics solution provider Manugistics, IKEA was able to forecast much more accurately, align production with demand projections, and in the end reduce inventory levels by over 20 percent[7]—money that could be reinvested in distribution systems and new product development and evaluation, among other projects.

ORDER FULFILLMENT

order fulfillment process
A supply chain management process that involves generating, filling, delivering, and providing on-the-spot service for customer orders.

order-to-cash cycle
The amount of time between order placement, receipt of the customer's payment, and order shipment.

third party logistics firm (3PL)
A firm that is contracted to manage part or all of another firm's order fulfillment process.

manufacturing flow management process
A process that ensures that firms in the supply chain have the resources they need.

One of the most fundamental processes in supply chain management is the order fulfillment process, which involves generating, filling, delivering, and providing on-the-spot service for customer orders. The order fulfillment process is a highly integrated process, often requiring persons from multiple companies and multiple functions to come together and coordinate to create customer satisfaction at a given place and time. The best order fulfillment processes reduce the time between order and customer receipt as much as possible, while ensuring that the customer receives exactly what he/she wanted. The shorter lead times are beneficial in that they allow firms to carry reduced inventory levels and free up cash that can be used on other projects. Activities in the order fulfillment process include working with salespeople to generate and enter orders, order processing and document handling, order filling and delivery, and updating account status following shipment. Overall, the order fulfillment process involves understanding both internal capabilities and external customer needs, and matching these together so that the supply chain maximizes profits while minimizing costs and waste.

When the order fulfillment process is managed diligently, the amount of time between order placement and receipt of the customer's payment following order shipment (known as the order-to-cash cycle) is minimized as much as possible. Since many firms do not view order fulfillment as a core competency (versus, for example, product development or marketing), they often outsource this function to a third party logistics firm (3PL) that specializes in the order fulfillment process. The 3PL becomes a semi-permanent part of the firm's supply chain assigned to manage one or more specialized functions. When employed for the purposes of order fulfillment, the 3PL is contracted to manage the firm's order fulfillment process from beginning to end, thereby freeing up the firm's time and resources so that they can be expended on core business activities.

MANUFACTURING FLOW MANAGEMENT

The manufacturing flow management process is concerned with ensuring that firms in the supply chain have the needed resources to manufacture with flexibility and to move products through a multi-stage production process. Firms with flexible manufacturing have the ability to create a wide variety of goods and/or services with minimized costs associated with changing production techniques. The manufacturing flow process includes much more than simple production of goods and services—it means creating flexible agreements with suppliers and shippers so that unexpected demand bursts can be accommodated. Activities in the manufacturing flow process include, but are not limited to, the determination of a supply's route and velocity through manufacturing; materials planning; inventory management and control for both parts and finished goods; and quality management.

The goals of the manufacturing flow management process are centered on leveraging the capabilities held by multiple members of the supply chain to improve overall manufacturing output in terms of quality, delivery speed, and flexibility, all of which tie to profitability. For instance, when GM changed over to flexible manufacturing in the early 2000s, managers and shareholders were pleased to discover that switching manufacturing facilities to accommodate different car model lines took only three days, as compared to the six weeks of downtime that was typical prior to the upgrade. GM executives estimate that the company has saved over $1.5 billion per year due to more efficient asset utilization. In addition, they have also added flexible robotics to a few plants (i.e., robots that can be reprogrammed and thereby adapted for use in more than one production process), at a further savings of $120 million.[8] These types of adjustments to firms' manufacturing flow process are illustrative of the enormous potential that fine-tuning the process could have for the firm's bottom-line.

SUPPLIER RELATIONSHIP MANAGEMENT

supplier relationship management process
A supply chain management process that supports manufacturing flow by identifying and maintaining relationships with highly valued suppliers.

product development and commercialization process
The group of activities that facilitates the joint development and marketing of new offerings among a group of supply chain partner firms.

The supplier relationship management process is closely related to the manufacturing flow management process and contains several characteristics that parallel the customer relationship management process. The manufacturing flow management process is highly dependent on supplier relationships for flexibility. Furthermore, in a way similar to that found in the customer relationship management process, supplier relationship management provides structural support for developing and maintaining relationships with suppliers. Thus, integrating these two ideas, supplier relationship management supports manufacturing flow by identifying and maintaining relationships with highly valued suppliers. Just as firms benefit from developing close-knit and integrated relationships with customers, close-knit and integrated relationships with suppliers provide a means through which performance advantages can be gained. Activities germane to the supplier relationship management process typically include identifying and selecting suppliers; creating supplier scoring criteria and applying scorecard tools to supplier groups; conducting periodic supplier reviews and visits; and identifying ways that suppliers could provide greater service levels at similar costs, among many others.

The management of supplier relationships is a key step toward ensuring that firms' manufacturing resources are available, and thereby the supplier relationship management process has a direct impact on each supply chain member's bottom-line financial performance. In fact, the manufacturing division of Toyota Motor Co. of America takes the supplier relationship management process so seriously that it established on-site offices for suppliers when opening a new truck plant in 2006. This seemingly drastic move was intended to fully integrate suppliers into the Toyota manufacturing process, including the ability for Toyota to monitor second-tier suppliers, practice on-site quality management, and lower transportation and operating costs.[9]

PRODUCT DEVELOPMENT AND COMMERCIALIZATION

The product development and commercialization process (discussed in detail in Chapter 11) includes the group of activities that facilitates the joint development and marketing of new offerings among a group of supply chain partner firms. In many cases, new products and services are not the sole responsibility of a single firm who serves as inventor, engineer, builder, marketer, and sales agent, but rather, they are often the product of a multi-company collaboration with multiple firms and business units playing unique roles in new product development, testing, and launch activities, among others. The capability for developing and introducing new offerings quickly is key for competitive success versus rival firms, and so it is often advantageous to involve many supply chain partners in the effort. Activities that are embedded within the product development and commercialization process commonly include new product idea generation and screening; cross-functional and cross-organization team assembly; product rollout requirement identification; and new offering profitability analysis. The process requires the close cooperation of suppliers and customers who provide input throughout the process and serve as advisors and co-producers for the new offering(s).

RETURNS MANAGEMENT

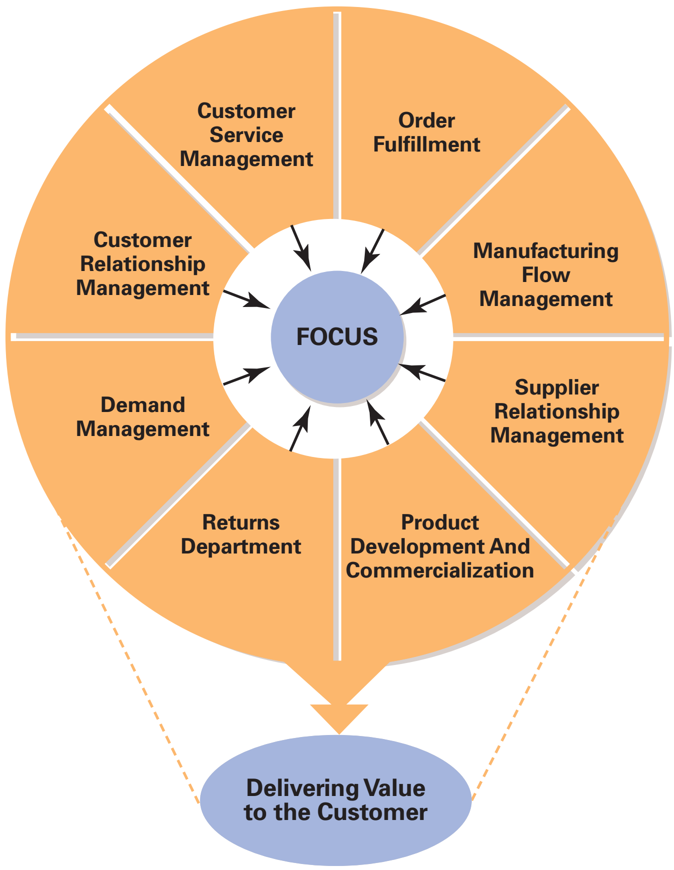
returns management process
A process that enables firms to manage volumes of returned product efficiently, while minimizing costs and maximizing the value of the returned assets to the firms in the supply chain.

The final supply chain management process deals with incidents where customers choose to return a product to the retailer or supplier, thus creating a reversed flow of goods within the supply chain. Returns occur for a variety of reasons, including customer dissatisfaction, slow sales or poor quality, asset recapture (i.e., reusable packaging), product recalls, and recycling. The returns management process enables firms to manage volumes of returned product efficiently, while minimizing returns related costs and maximizing the value of the returned assets to the firms in the supply chain. Though this process would seem to be less important than supply chain activities occurring under "normal" circumstances, it is worth considering that though returns average about 6 percent of sales in most cases, they do reach up to 40 percent of sales volume in certain industries such as apparel e-retailing. Thus, the activities associated with returns management have the potential to impact the firm's financial position in a major and negative way if mishandled. Activities commonly associated with the returns management process include returns gatekeeping (determination of whether a return is allowed for a product in question), returns routing, deciding on how to dispose of the returned product, and re-crediting or reconciliation of the customer's account.

In addition to the value of managing returns from a pure asset-recovery perspective, many firms are discovering that returns management also creates additional marketing and customer service touch points that can be leveraged for added customer value above and beyond normal sales and promotion-driven encounters. Handling returns gives the company an additional opportunity to please the customer, and customers who have positive experiences with the returns management process can become very confident buyers who are willing to reorder, since they know any problems they encounter with purchases will be quickly and fairly rectified. In addition, the returns management process allows the firm to recognize weaknesses in product design and/or areas for potential improvement through the direct customer feedback that initiates the process.

REVIEW LEARNING OUTCOME

LO3 Identify the eight key processes of excellent supply chain management and discuss how each of these processes impacts the end customer



LO4

Strategic Supply Chain Management Decisions

The establishment of supply chain integration and identification of key business processes make world-class supply chain management possible for businesses. However, to take advantage of these principles, supply chain managers must implement them in practice. Supply chain management strategies guide the implementation of key supply chain management principles. When implementing supply chain management, a number of strategic questions are relevant, and these must be answered by managers who are seeking to gain the benefits of the integrated, process-oriented supply chain. Some of the most important questions are:

- Based on the markets we compete in, the suppliers available, and the products we sell, what overarching supply chain strategy is most appropriate for my firm or business unit?
- What does the overall "map" of all of the firm's key supply chain members look like?

These strategic questions are among the most major that supply chain managers will answer as they steer the firm toward operational and financial successes.

SUPPLY CHAIN STRATEGIES

Because products and marketplaces may differ substantially in their core characteristics from place to place and product to product, supply chain management strategies should be selected according to the situation at hand. In addition, because in many cases supply chains operate on a global scale, with far-away suppliers and customers communicating with, serving, or depending on local firms, companies must take care to adopt supply chain management strategies that strike a balance between the lower costs offered through global supply chain management and the assuredness of top-quality service that more localized solutions may provide.

One of the most interesting issues that supply chain managers face in this regard has to do with the mind-set of the firm. Most firms must choose between two strategic philosophies: high responsiveness to customers at any cost, or profitability through waste reduction (and therefore cost reduction) even if it means sometimes disappointing customers. These strategic philosophies are often referred to collectively in what has come to be known as the "lean" versus "agile" debate. The lean supply chain management strategy embraces the removal of waste from the supply chain system in whatever form it may be found. Made famous by Toyota production engineer Taiichi Ohno, the lean strategy seeks to remove any excesses from the supply chain, including overproduction, product defects, excess inventories, unneeded processing, movement of people, transport of goods, or employee idling. In lean companies, these principles are sometimes adhered to even if it means disappointing a small customer segment that wants more customized services. The implementation of lean supply chain principles launched Toyota into the upper echelon of automakers in terms of performance and profitability, and has caused this strategy, when properly implemented, to become viewed as a major strategic weapon. Benetton, the Italian clothing company, has also used lean principles when reviving its brand in recent years. By narrowing its product lines through the removal of the sportswear category, outsourcing the production of high-margin accessories to China, building an extensive worldwide distribution network, and breaking up inventory into smaller, quickly dispatched shipments, the company posted its highest levels of profitability in several years during 2006.[10]

lean supply chain management
The strategy that focuses primarily on the removal of waste from the supply chain to achieve the lowest total cost to the members of the supply chain system.

However, lean supply chain management obviously has weaknesses as a competitive strategy. Though "going lean" works well in situations where the advantages generated by mass manufacturing are present, such as cases where relatively stable and predictable market demand and low variety of customer preferences exist, the lean strategy does not work as well when customers prefer more customized products and when demand is more unpredictable. Thus, in contrast to lean supply chain management, other companies sometimes choose to adopt agile supply chain management strategies. Whereas the lean strategy is mostly concerned with waste reduction, the agile strategy is concerned primarily with customer responsiveness, and focuses primarily on the ability of the firm to fulfill demand in situations where consumer wants and needs are less obvious. A key concept for the implementation of agile SCM is the notion of flexibility. Instead of relying on forecasts that drive production ahead of demand, agile supply chains adopt a wait-and-see approach where commitment to supply chain processes is unknown until the order is placed. They then make products customized to order specifications. With the agile strategy, the customer is always right, and is to be served to the utmost even if this means somewhat higher costs.

agile supply chain management
The supply chain strategy that focuses primarily on the ability of the firm to fulfill customer demand, even if this means somewhat higher costs.

Leagile supply chain strategy
A supply chain management strategy that combines the best elements of the lean and agile strategies for a particular product/market combination.

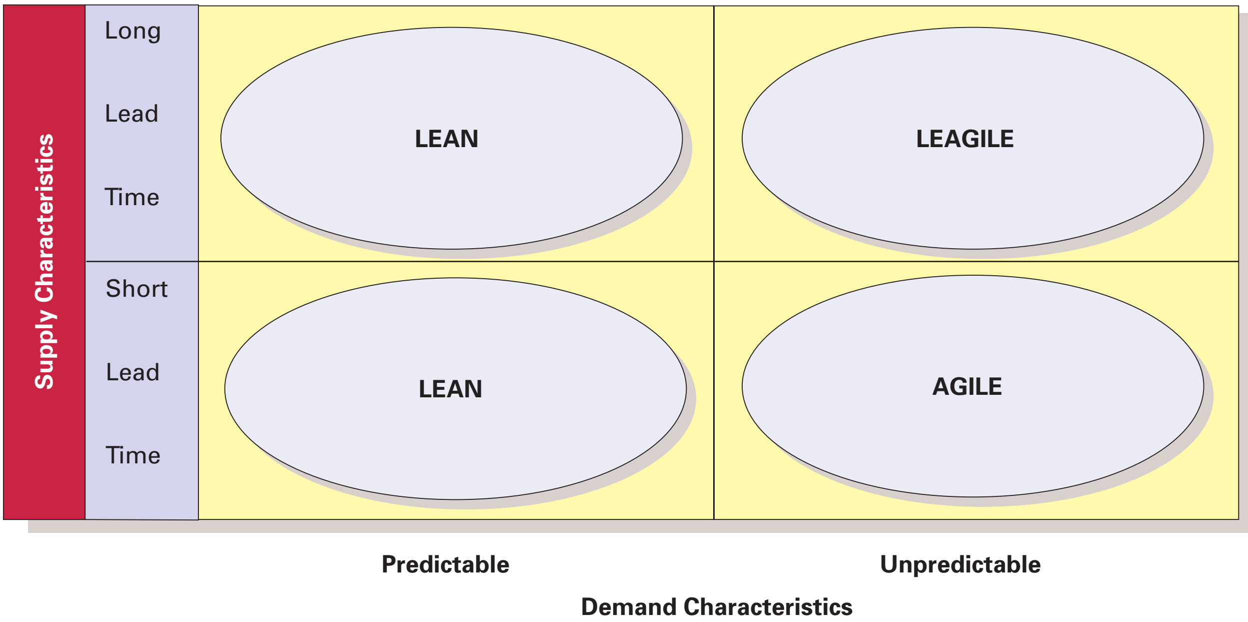
postponement
The delay in final production in the Leagile supply chain management strategy that enables the company to take advantage of many of the benefits of lean supply chain management while still providing the agility that improves customer experiences.

Though the lean and agile supply chain strategies may at first seem to include opposing perspectives and actions, this is not necessarily always the case. First, the two strategies do, in fact, share a common objective: to fulfill customer requirements at the lowest total cost to the members of the supply chain system. (The difference is at what point the firm determines that cost control becomes more important than customer demands. With the lean strategy, cost control becomes a priority much sooner, and with the agile strategy, customer focus remains the key much longer.) Because of this common goal, some of the elements of each strategy can be combined in a hybrid strategy. The bringing together of principles from each of the main strategic viewpoints has been termed a Leagile supply chain strategy. With the Leagile strategy, the best elements of each strategy for the particular product/market combination describing the firm are selected. For example, customers wishing to purchase a Toyota Scion can log onto the company website and build their car to a highly customized degree, including the selection of leather versus cloth seats, many different wheel types, and a wide variety of sound and video equipment. However, the base automobile is manufactured and shipped from within Japan using lean principles; only later are the "agile" components selected by the customer installed, with the final customization often occurring at the local dealership location. This delay in final production is called postponement. Through postponement, the Leagile supply chain management strategy allows the company to take advantage of many of the benefits of lean supply chain management while still providing the agility that makes many customer experiences more desirable.

The big question then is under what conditions companies should use lean, agile, and/or Leagile supply chain management strategies? The answer to this question depends largely on the characteristics of the supply market and customer demand for the product. In situations where aggregate customer demand is predictable, it is generally accepted that lean supply chain management offers the greatest benefits in terms of waste reduction associated with repetitive manufacturing flow and order fulfillment processes. However, when customer demand is less certain, the best supply chain management strategy to choose depends on supply market characteristics. Specifically, when there are an abundance of suppliers, and the supply market as a whole is quick and responsive, an agile strategy is usually best because it maximizes customer responsiveness at the lowest levels of risk. On the other hand, when the supply market is less certain, the firm may be better off implementing a Leagile strategy, with some generic inventory being held at strategic locations ready for quick customer adaptation and sale. These situations are depicted in Exhibit 14.3.

Exhibit 14.3

Lean versus Agile Supply Chain Management



SOURCE: Martin Christopher, Helen Peck, and Denis Towill, "A Taxonomy for Selecting Global Supply Chain Stategies" (2007), *International Journal of Logistics Management*, Vol. 17, No. 2, pp. 277–287.

MAPPING THE SUPPLY CHAIN

In addition to the selection and implementation of an overarching supply chain management strategy, firms must also understand the structure of their supply chain and the many relationships existing between members. In terms of their structure, all supply chains may be viewed as groupings of nodes and linkages, with the nodes being firms or business units/functions, and the links being the processes that connect them. A typical supply chain network looks like an uprooted tree laid upon its side, as shown in Exhibit 14.4. Viewing this exhibit, decisions related to supply chain structure are centered on which nodes should be included in the network and what level or degree of linkage should be used to connect any two nodes. With respect to the first question, firms consider issues such as how long the supply chain for a product should be and what number of suppliers or customers should be included in each level of the network. For example, many firms seek to "optimize" their collection of suppliers (supply base) by including only the certain number of suppliers that can be adequately managed through personal relationships, given that the amount of resources the firm has available to expend on this task is limited. Three dimensions of supply chain network design are commonly considered by supply chain managers: the horizontal structure, the vertical structure, and the horizontal position. The horizontal structure is the number of tiers (rows in the supply chain representing the total number of levels through which goods and services must pass from the earliest to end stages of the chain). The vertical structure is the number of suppliers or customers included within each individual tier. Given a particular horizontal and vertical structure, the horizontal position of the firm can be established. The firm can be at or near the beginning (origin), end (customer), or anywhere between in the supply chain. The horizontal position of the firm is important to establish, as firms that are located near one end of the supply chain often find it very challenging to manage processes that are located closer to the other end.

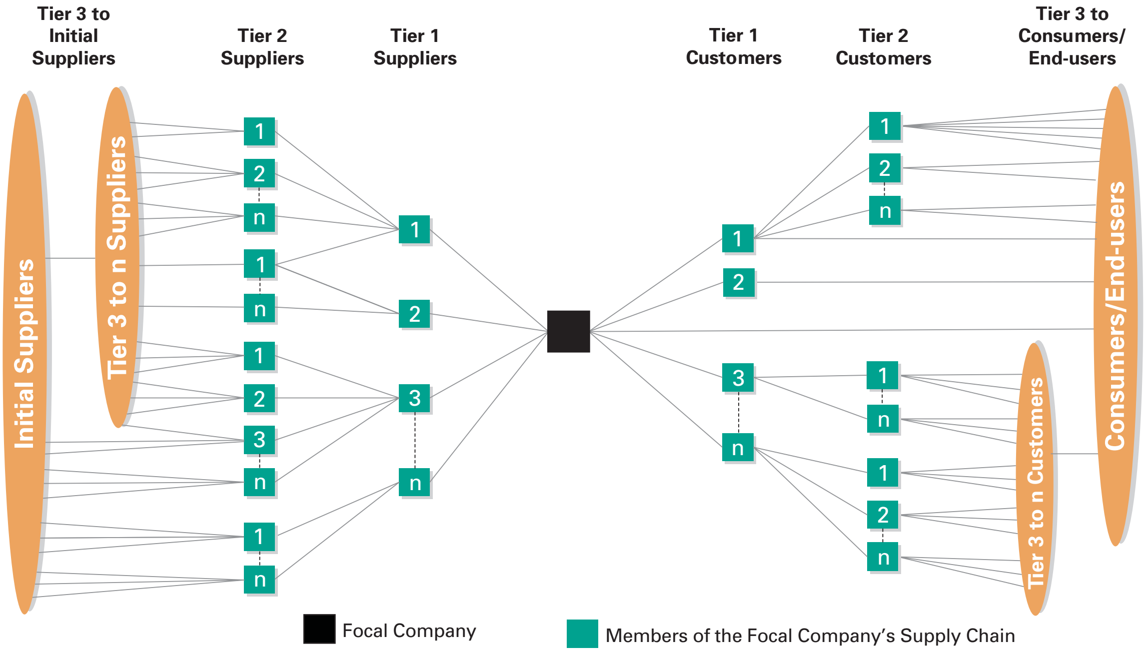
horizontal structure
One of three dimensions of supply chain network design; the number of tiers (columns) in the supply chain, representing the total number of levels through which goods and services must pass from the earliest to end stages of the chain.

vertical structure
One of three dimensions of supply chain network design; the number of suppliers or customers included within each individual tier.

horizontal position
One of three dimensions of supply chain network design; the position of a firm, relative to other firms, along the supply chain.

Exhibit 14.4

A Supply Chain Network Map



SOURCE: Douglas M. Lambert, Editor, *Supply Chain Management: Processes, Partnerships, Performance,* Third Edition, Sarasota, FL: Supply Chain Management Institute, 2008, p. 6 adapted from Douglas M. Lambert, Martha C.Cooper, and Janus D. Pagh, "Supply Chain Management Implementation Issues and Research Opportunities," *The International Journal of Logistics Management,* Vol. 9, No. 2, 1998, p. 3. Copyright 2008, Supply Chain Management Institute. For more information see: www.scm-institute.org

GLOBAL Perspectives

We'll Bring the Work to You

Over the last several years, much has been publicized about Western nations' outsourcing of low-tech, unskilled jobs to places such as India and Africa as a strategy for achieving lower labor costs. Though lesser known and discussed, firms in the United States have also begun to export high-tech professional positions, and the country of destination may be a surprise to some: Canada. Citing less restrictive immigration policies as a primary motivator, Microsoft recently relocated a 700-employee software development center from its headquarters in Washington State to Richmond, British Columbia. Richmond is a suburb of Vancouver, BC, which is the largest city on the Canadian west coast.

The move to Richmond was deemed necessary by Microsoft executives because of difficulties its foreign workers were having in acquiring US H1-B work visas. Microsoft relies on a significant number of skilled engineers and other professionals from Southeast Asia in producing its software products. Canada was attractive to Microsoft because the nation has no cap on foreign worker visas issued by its federal government, whereas Microsoft workers from Asia settling in Washington state were often denied visas due to U.S. immigration caps or quotas. Furthermore, U.S. immigrants who are approved sometimes have to wait 5-6 years to get a green card. Canada's expedited process results in visas being issued to some workers in under two weeks, with no requirement for workers to seek future citizenship.

Complaints made by Microsoft and others to the U.S. Senate about recent shortages of the H1-B visas went largely unheralded, and in combination with failed immigration reform legislation, forced the company to re-evaluate the optimal location for its software development process. Upon hearing about Microsoft's quandary, Canada was quick to react, broadcasting a broad message of welcome for US companies seeking to relocate skilled positions north of the border. Thus, the assumption that high-tech, skilled U.S. workers are protected from job loss due to outsourcing is somewhat tenuous. As one member of the Washington Alliance of Technology Workers put it, "Companies want to find out . . . who can do the work cheapest, and they move their facilities around the globe to do that . . . it's simply a myth that white collar jobs are too complex, too difficult for their companies to outsource." As Microsoft has shown, some American companies are willing and able to do just that.[11]

Do you think American firms should outsource white collar jobs to other countries? Why or why not? How does expanding the supply chain network across nations create advantages or disadvantages for the members of the supply chain?

REVIEW LEARNING OUTCOME

LO4 Discuss the key strategic decisions supply chain managers must make when designing their companies' supply chains

Lean firms focus on improving profitability through the removal of waste from the supply chain system.

Agile firms seek to provide the highest levels of customer responsiveness and service possible, even if the costs of doing so are higher.

Leagile firms adopt a position somewhere in between, with main components made and shipped using lean principles, but with agility gained later through the postponement of final production.

LO5

The Logistics Function in the Supply Chain

Now that you are familiar with the structure and strategy of supply chain management, it is important to also understand the physical means through which products move through the supply chain. As mentioned earlier, supply chain management coordinates and integrates all of the activities performed by supply chain members into a seamless process. The logistics function of the supply chain is responsible for the movement and delivery of goods and services into, through, and out of each firm in the supply chain network. The logistics function consists of several interrelated and integrated logistical components: (1) sourcing and procurement of raw materials and supplies, (2) order processing, (3) inventory management and control, (4) warehousing and materials-handling, and (5) transportation.

logistics information system The link that connects all of the logistics components of the supply chain.

supply chain team An entire group of individuals who orchestrate the movement of goods, services, and information from the source to the consumer.

A logistics information system provides the technological link connecting all of the logistics components of the supply chain. The components of the system include, for example, software for materials acquisition and handling, warehouse-management and enterprise-wide solutions, data storage and integration in data warehouses, mobile communications, electronic data interchange, RFID chips, and the Internet. Working together, the components of the logistics information system are the fundamental enablers of successful supply chain management.

The supply chain team, leveraging the capabilities of the logistics information system, orchestrates the movement of goods, services, and information from the source to the consumer. Supply chain teams typically cut across organizational boundaries, embracing all parties who participate in moving the product to market. The best supply chain teams also move beyond the organization to include the external participants in the chain, such as suppliers, transportation carriers, and third-party logistics suppliers. Members of the supply chain communicate, coordinate, and cooperate extensively to make the logistics function as efficient and effective as possible.

Today's corporate supply chain logisticians have become so efficient that the U.S. Marine Corps is now consulting with companies like Wal-Mart, UPS, and Unilever to improve its own supply chain efficiency. The Marine Corps's goal is to reduce the time it takes to deliver supplies to the front lines from one week to 24 hours and lower costs by cutting inventories in half.

SOURCING AND PROCUREMENT

One of the most important links in the supply chain is the one between the manufacturer and the supplier. Purchasing professionals are on the front lines of supply chain management. Purchasing departments plan purchasing strategies, develop specifications, select suppliers, and negotiate price and service levels. Often, goods are procured for use in local manufacturing processes from suppliers halfway around the world. This is especially true for the United States, which was the world's top importer in 2007, with nearly $2 trillion worth of purchased merchandise entering the nation through its international ports.[12]

The goal of most sourcing and procurement activities is to reduce the costs of raw materials and supplies. Purchasing professionals have traditionally relied on tough negotiations to get the lowest price possible from suppliers of raw materials, supplies, and components. Perhaps the biggest contribution purchasing can make to supply chain management, however, is in the area of vendor relations. Companies can use the purchasing function to strategically manage suppliers in order to reduce the total cost of materials and services. Through enhanced vendor relations, buyers and sellers can develop cooperative relationships that reduce costs and improve efficiency with the aim of lowering prices and enriching profits. By integrating suppliers into their companies' businesses, purchasing managers have become better able to streamline purchasing processes, manage inventory levels, and reduce overall costs of the sourcing and procurement operations.

ORDER PROCESSING

order processing system
A system whereby orders are entered into the supply chain and filled.

electronic data interchange (EDI)
Information technology that replaces the paper documents that usually accompany business transactions, such as purchase orders and invoices, with electronic transmission of the needed information to reduce inventory levels, improve cash flow, streamline operations, and increase the speed and accuracy of information transmission.

The order is often the catalyst that sets the supply chain in motion, especially in the build-to-order environments of leading computer manufacturers such as Dell. The order processing system processes the requirements of the customer and sends the information into the supply chain via the logistics information system. The order goes to the manufacturer's warehouse. If the product is in stock, the order is filled and arrangements are made to ship it. If the product is not in stock, it triggers a replenishment request that finds its way to the factory floor.

The role of proper order processing in providing good service cannot be overemphasized. As an order enters the system, management must monitor two flows: the flow of goods and the flow of information. Often marketers' best-laid plans get entangled in the order processing system. Obviously, good communication among sales representatives, office personnel, and warehouse and shipping personnel is essential to correct order processing. Shipping incorrect merchandise or partially filled orders can create just as much dissatisfaction as stockouts or slow deliveries. The flow of goods and information must be continually monitored so that mistakes can be corrected before an invoice is prepared and the merchandise shipped.

Order processing is becoming more automated through the use of computer technology known as electronic data interchange (EDI). The basic idea of EDI is to replace the paper documents that usually accompany business transactions, such as purchase orders and invoices, with electronic transmission of the needed information. A typical EDI message includes all the information that would traditionally be included on a paper invoice such as product code, quantity, and transportation details. The information is usually sent via private networks, which are more secure and reliable than the networks used for standard e-mail messages. Most importantly, the information can be read and processed by computers, significantly reducing costs and increasing efficiency. Companies that use EDI can reduce inventory levels, improve cash flow, streamline operations, and increase the speed and accuracy of information transmission. EDI also creates a closer relationship between buyers and sellers.

It should not be surprising that retailers have become major users of EDI. For Wal-Mart, Target, and the like, logistics speed and accuracy are crucial competitive tools in an overcrowded retail environment. Many big retailers are helping their suppliers acquire EDI technology so that they can be linked into the system. EDI works hand in hand with retailers' *efficient consumer response* programs, which are designed to have the right products on the shelf, in the right styles and colors, at the right time, through improved inventory, ordering, and distribution techniques. (See Chapter 15 for more discussion of retailers' use of EDI techniques.)

INVENTORY MANAGEMENT AND CONTROL

Closely interrelated with the procurement, manufacturing, and ordering processes is the inventory control system—a method that develops and maintains an adequate assortment of materials or products to meet a manufacturer's or a customer's demands.

inventory control system
A method of developing and maintaining an adequate assortment of materials or products to meet a manufacturer's or a customer's demand.

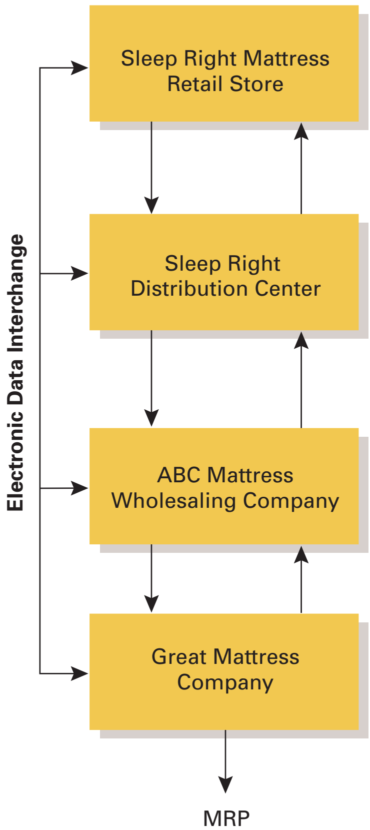
materials requirement planning (MRP) (materials management)
An inventory control system that manages the replenishment of raw materials, supplies, and components from the supplier to the manufacturer.

distribution resource planning (DRP)
An inventory control system that manages the replenishment of goods from the manufacturer to the final consumer.

Inventory decisions, for both raw materials and finished goods, have a big impact on supply chain costs and the level of service provided. If too many products are kept in inventory, costs increase—as do risks of obsolescence, theft, and damage. If too few products are kept on hand, then the company risks product shortages and angry customers, and ultimately lost sales. For example, negative sales forecasts for the Christmas buying season in the past few years caused many retailers to cut back on orders because they were afraid of having to discount large end-of-the-year inventories. As a result, many companies, including Panasonic and Lands' End, lost sales due to inventory shortages on popular items. The goal of inventory management, therefore, is to keep inventory levels as low as possible while maintaining an adequate supply of goods to meet customer demand.

Managing inventory from the supplier to the manufacturer is called materials requirement planning (MRP), or materials management. This system also encompasses the sourcing and procurement operations, signaling purchasing when raw materials, supplies, or components will need to be replenished for the production of more goods. The system that manages the finished goods inventory from manufacturer to end user is commonly referred to as distribution resource planning (DRP). Both inventory systems use various inputs, such as sales forecasts, available inventory, outstanding orders, lead times, and mode of transportation to be used, to determine what actions must be taken to replenish goods at all

Exhibit 14.5
Inventory Replenishment Example



Sleep Right is planning a promotion on the Great Mattress Company's Gentle Rest mattress. Sales forecast is for 50 units to be sold. Sleep Right has 10 open Gentle Rest orders with its distribution center. New mattresses must be delivered in two weeks in time for the promotion.

Sleep Right's Distribution Center is electronically notified of the order of 50 new Gentle Rest mattresses. It currently has 20 Gentle Rest mattresses in inventory and begins putting together the transportation plans to deliver these to the Sleep Right Store. Delivery takes one day. It orders 40 new mattresses from its mattress wholesaler to make up the difference.

ABC Mattress Wholesaling Company is electronically notified of Sleep Right DC's order of 40 new Gentle Rest mattresses. It currently does not have any of these in stock but electronically orders 40 from the Great Mattress Company's factory. Once it receives the new mattresses, it can have them delivered to the Sleep Right DC in two days.

The Great Mattress Company electronically receives ABC's order and forwards it to the factory floor. Production of a new mattress takes 20 minutes. The total order of 40 mattresses can be ready to be shipped to ABC in two days. Delivery takes one day. Raw material supplies for this order are electronically requested from Great Mattress's supply partners, who deliver the needed materials just-in-time to its stitching machines.

points in the supply chain. Demand in the system is collected at each level in the supply chain, from the retailer back up the chain to the manufacturer. With the use of electronic data interchange, the information can be transmitted much faster to meet the quick-response needs of today's competitive marketplace. Exhibit 14.5 provides an example of inventory replenishment using DRP from the retailer to the manufacturer.

automatic replenishment program
An inventory management system that triggers shipments only once a good is sold to the customer; the program uses EDI linkage connected with barcode scanners at the point of purchase, so the supplier can view the inventory being held at the next tier of the supply chain in real time.

materials-handling system
A method of moving inventory into, within, and out of the warehouse.

Other inventory management systems that have gained in popularity in recent years, however, use few or no forecasts at all during the scheduling of shipments. Known as automatic replenishment programs, these systems trigger shipments only once a good (usually something with a relatively predictable demand pattern) is sold to the customer. Using an EDI linkage connected with barcode scanners at the point of purchase, the supplier can view the inventory being held at the next tier of the supply chain in real time. When stock of a good at the customer location falls below pre-established safety levels, orders are automatically packed and shipped from the supplier location. Thus, in this type of system, the supplier takes responsibility for keeping inventory on the shelves or in the customer's warehouse; this usually results in reduced stockouts and lowers overall inventory levels.

WAREHOUSING AND MATERIALS-HANDLING

Supply chain logisticians oversee the constant flow of raw materials from suppliers to manufacturer and finished goods from the manufacturer to the ultimate consumer. Although build-to-order manufacturing processes may eliminate the need to warehouse many raw materials, manufacturers may often keep some safety stock on hand in the event of an emergency, such as a strike at a supplier's plant or a catastrophic event that temporarily stops the flow of raw materials to the production line. Likewise, the final user may not need or want the goods at the same time the manufacturer produces and wants to sell them. Products like grain and corn are produced seasonally, but consumers demand them year-round. Other products, such as Christmas ornaments and turkeys, are produced year-round, but consumers do not want them until autumn or winter. Therefore, management must have a storage system to hold these products until they are shipped.

Storage is what helps manufacturers manage supply and demand, or production and consumption. It provides time utility to buyers and sellers, which means that the seller stores the product until the buyer wants or needs it. Even when products are used regularly, not seasonally, many manufacturers store excess products in case the demand surpasses the amount produced at a given time. Storing additional product does have disadvantages, however, including the costs of insurance on the stored product, taxes, obsolescence or spoilage, theft, and warehouse operating costs. Another drawback is opportunity costs—that is, the opportunities lost because money is tied up in stored product instead of being used for something else.

Because businesses are focusing on cutting supply chain costs, the warehousing industry is also changing to better serve its customers. For example, many warehouses are putting greater emphasis on more efficient unloading and reloading layouts and customized services that move merchandise through the warehouse faster, often in the same day. They also are investing in services using sophisticated tracking technology such as materials-handling systems.

A materials-handling system moves inventory into, within, and out of the warehouse. Materials-handling includes these functions:

- Receiving goods into the warehouse or distribution center
- Identifying, sorting, and labeling the goods

- Dispatching the goods to a temporary storage area
- Recalling, selecting, or picking the goods for shipment (may include packaging the product in a protective container for shipping)

The goal of the materials-handling system is to move items quickly with minimal handling. With a manual, non-automated materials-handling system, a product may be handled more than a dozen times. Each time it is handled, the cost and risk of damage increase; each lifting of a product stresses its package. Consequently, most manufacturers today have switched to automated systems. Scanners quickly identify goods entering and leaving a warehouse through bar-coded labels affixed to the packaging. Electronic storage and retrieval systems automatically store and pick goods in the warehouse or distribution center. Automated materials-handling systems decrease product handling, ensure accurate placement of product, and improve the accuracy of order picking and the rates of on-time shipment. In fact, many firms are coming to rely on materials handling systems operated either partially, or in rare cases fully, by robots. Since 2006, this has been the case at office supply giant Staples, where over 150 robots collect materials for, process, and pack up to 8,000 orders daily.[13]

At Dell, the OptiPlex system runs the factory. The computer software receives orders, sends requests for parts to suppliers, orders components, organizes assembly of the product, and even arranges for it to be shipped. Thus, instead of hundreds of workers, often fewer than six are working at one time. An order for a few hundred computers can be filled in less than eight hours using the automated system. With the OptiPlex system, productivity has increased 160 percent per person per hour.[14]

TRANSPORTATION

Transportation typically accounts for 5 to 10 percent of the price of goods. Supply chain logisticians must decide which mode of transportation to use to move products from supplier to producer and from producer to buyer. These decisions are, of course, related to all other logistics decisions. The five major modes of transportation are railroads, motor carriers, pipelines, water transportation, and airways. Supply chain managers generally choose a mode of transportation on the basis of several criteria:

- *Cost:* The total amount a specific carrier charges to move the product from the point of origin to the destination
- *Transit time:* The total time a carrier has possession of goods, including the time required for pickup and delivery, handling, and movement between the point of origin and the destination
- *Reliability:* The consistency with which the carrier delivers goods on time and in acceptable condition
- *Capability:* The ability of the carrier to provide the appropriate equipment and conditions for moving specific kinds of goods, such as those that must be transported in a controlled environment (for example, under refrigeration)
- *Accessibility:* A carrier's ability to move goods over a specific route or network
- *Traceability:* The relative ease with which a shipment can be located and transferred

The mode of transportation used depends on the needs of the shipper, as they relate to these six criteria. Exhibit 14.6 compares the basic modes of transportation on these criteria.

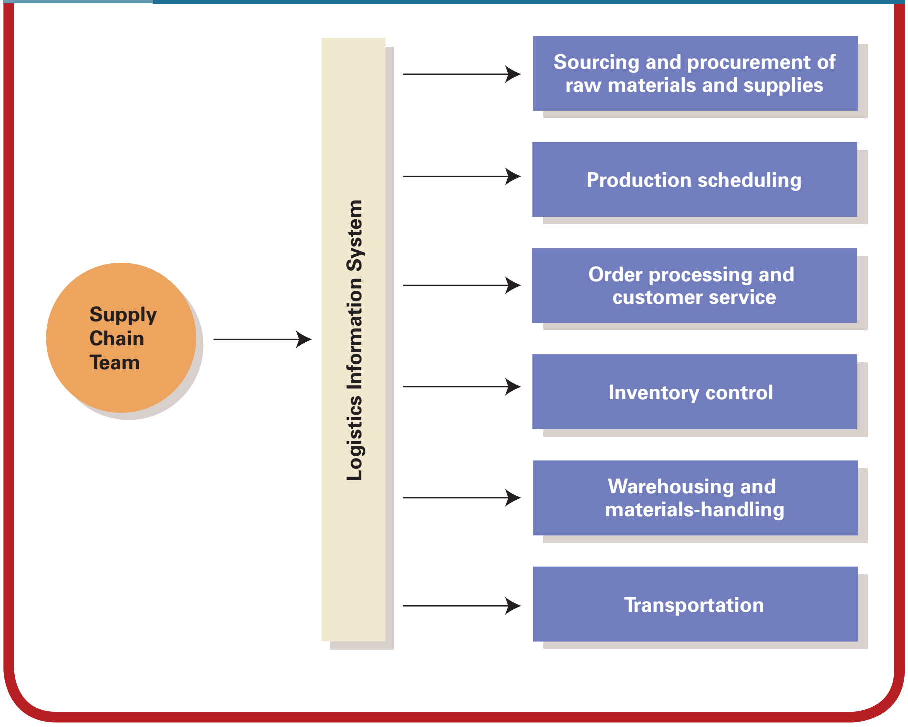
Exhibit 14.6

Criteria for Ranking Transportation Modes

	Highest				Lowest
Relative Cost	Air	Truck	Rail	Pipe	Water
Transit Time	Water	Rail	Pipe	Truck	Air
Reliability	Pipe	Truck	Rail	Air	Water
Capability	Water	Rail	Truck	Air	Pipe
Accessibility	Truck	Rail	Air	Water	Pipe
Traceability	Air	Truck	Rail	Water	Pipe

REVIEW LEARNING OUTCOME

LO 5 Describe the logistical components of the supply chain



LO 6 Supply Chain Performance Measurement

A commonly repeated saying in business is, “That which cannot be measured, cannot be managed.” This adage is especially true in the case of supply chain management, where multiple processes, each composed of different types of activities, are operated simultaneously with the goal of enhancing the performance of the business. Firms that are able to develop a well thought out system of supply chain measurement procedures are able to constantly monitor their processes, can see where they are doing well in addition to where they are failing, and are best able to gain a competitive advantage though better service and lower costs.

Because supply chains can be very complex and information is not always visible across firms operating in the same supply chain, many of the ways that managers try to measure their success or failure are not always reflective of the chain as a whole; many firms use measures of logistics performance for their own firm (such as on-time delivery rates, order cycle time, or inventory turnover) as proxies for the performance of the whole chain. However, recalling that a primary goal of supply chain management is the optimization of the entire system rather than any single firm within it, many companies are seeking to develop new metrics that will allow them a broader and more comprehensive viewpoint from which to study their supply chain’s efficiency and effectiveness. Metrics are standard measures that can be used repeatedly to assess performance on a supply chain-related process. Common examples of metrics might include customer satisfaction ratings, orders picked from the warehouse per hour, or the ratio of operating assets to income. From the perspective of the supply chain manager, a good metric is characterized by five qualities:

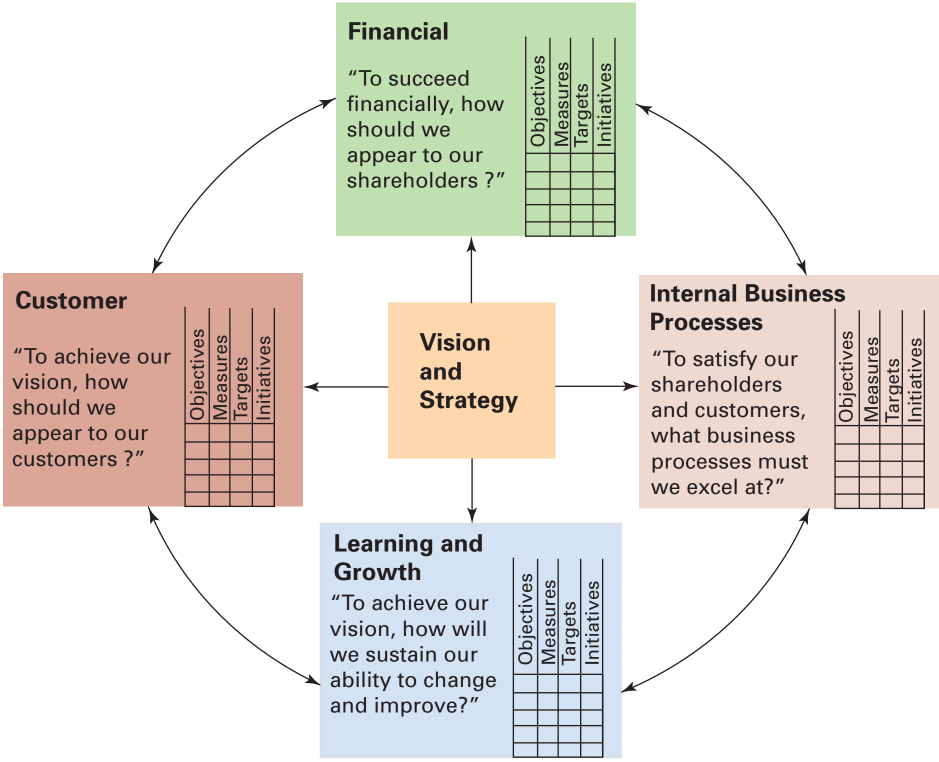
metrics
Standard measures that can be used repeatedly to assess performance on a supply chain-related process.

- It creates understanding of strategic objectives and tactical plans.
- It promotes behaviors that are consistent with achieving these objectives.
- It allows for recording of actual results/outcomes, and therefore the firm can monitor progress toward objectives.
- It allows companies to compare themselves to competitors (or benchmarks) and customer expectations.
- It motivates continuous improvement.

For firms using the logistics-proxy approach to supply chain measurement, several measures are often used across four unique categories of performance. The performance categories are customer satisfaction, time, cost, and asset utilization. Customer satisfaction measures often include metrics such as order fulfillment, satisfaction ratings taken from questionnaires, on-time deliveries, number of returned products, or

Exhibit 14.7

Balanced Scorecard Approach to Performance Measurement



Source: From www.balancedscorecard.org.

length of delay in executing customer service activities. Time measures often employ metrics such as order-to-receipt time or source-to-make cycle time. Cost measures are often calculated as the total aggregate costs of the supply chain (on an activity basis) for a good or service, from creation through delivery. Asset utilization metrics frequently include days of inventory supply, asset performance ratios, or forecast accuracy, to name a few.

THE BALANCED SCORECARD APPROACH

Because supply chain management is concerned with the performance of all firms in the system simultaneously, any performance measurement system used to evaluate a supply chain must address both the chain itself and all of the processes and firms that compose it. One method developed for this purpose is known as the Balanced Scorecard Approach. This approach, invented by Robert S. Kaplan and David P. Norton of Harvard Business School, combines multiple different categories of measurements that can be used at all levels of the supply chain. The Balanced Scorecard Approach is shown pictorially in Exhibit 14.7.

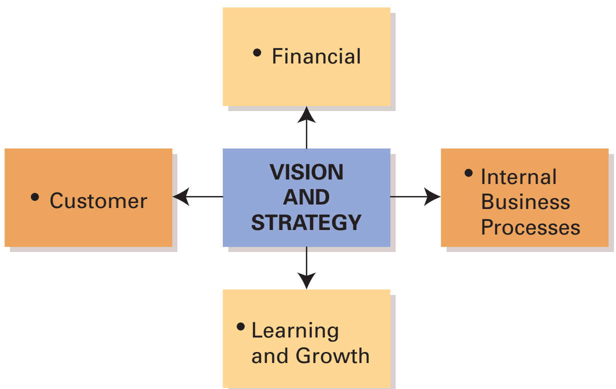
Balanced Scorecard Approach
A measurement system used to evaluate overall supply chain performance.

The Balanced Scorecard Approach is an effective method for assessing overall supply chain performance because it implicitly includes the linkage between the supply chain strategy adopted by the firm in conjunction with the processes undertaken to fulfill it. By using the Balanced Scorecard, firms gain different types of feedback related to their supply chain operations, including strategic data for high-level decision makers, diagnostic feedback to guide process improvement, knowledge of trends in important metrics over time, feedback on the effectiveness of the performance measurements themselves, and data that can be used for forecasting future business activities.[15]

At each tier of the supply chain, the Balanced Scorecard addresses four areas of performance that are reflective of supply chain operations: customer-related performance metrics, financial metrics, learning and growth metrics, and of course, business process metrics. Firms take repeated measurements in each of these categories, and then alternate though a system whereby they do things to improve lagging performance in weak areas, check the results following implementation of changes, and act again based on new measurements.

REVIEW LEARNING OUTCOME

LO 6 Explain why supply chain performance measurement is necessary and important



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The multitude of global trade rules is why multinational companies like Eastman Kodak are so committed to working through the World Trade Organization to develop a global set of rules and to encourage countries to participate.

LO7

Trends in Supply Chain Management

Several technological advances and business trends are affecting the job of the supply chain manager today. Four of the most important trends are the globalization of supply chain management, advanced computer technology, outsourcing of logistics functions, and electronic distribution.

GLOBAL SUPPLY CHAIN MANAGEMENT

As global trade becomes a more decisive factor in success or failure for firms of all sizes, global supply chain management increases in importance. One of the most critical global supply chain issues for importers of any size is coping with the legalities of trade in other countries. Companies must be aware of the permits, licenses, and registrations they may need to acquire and, depending on the type of product they are importing, the tariffs, quotas, and other regulations that apply in each country. This multitude of different rules is why multinational companies like Eastman Kodak are so committed to working through the World Trade Organization to develop a global set of rules and to encourage countries to participate. Other goals for these companies include reducing trade barriers, such as tariffs. As these barriers fall, the flow of merchandise across borders is increasing due to more companies sourcing from multiple countries. For instance, a Kodak camera sold in France may have been assembled there, but the camera mechanism probably came from China and the film from the United States.

The presence of different rules hasn't slowed the spread of supply chain globalization, however. In spite of the added costs associated with importing and exporting goods, many companies are looking to other countries for their sourcing and procurement needs. For example, Applica, Inc., a U.S. maker of small appliances, is committed to using technology to improve its relationships with suppliers in Mexico. The company has linked its suppliers directly to sales data from Wal-Mart stores to help manage production and inventory costs.[16] In another case, United States soap producers faced with increased prices for a key ingredient due to new government legislation were forced to look for substitutes in Indonesia and Malaysia in order to remain profitable.[17]

Transportation can also be a major issue for companies dealing with global supply chains. Uncertainty regarding shipping usually tops the list of reasons why companies, especially smaller ones, resist international markets. Even companies that have scored overseas successes often are vulnerable to logistical problems. Large companies have the capital to create global logistics systems, but smaller companies often must rely on the services of carriers and freight forwarders to get their products to overseas markets.

In some instances, poor infrastructure makes transportation dangerous and unreliable. And the process of moving goods across the borders of even the most industrialized nations can still be complicated by government regulations. For example, NAFTA was supposed to improve the flow of goods across the continent, but moving goods across the border still requires approvals from dozens of government agencies, broker intervention, and hours spent at border checks. Shipping companies like Ryder are working to make the process easier. Currently, Ryder operates a cross-border facility in San Antonio to help clients like General Motors and Xerox with customs and logistics costs. The company also is part of a pilot project to automate border crossings with technology similar to that of an E-Z pass. The new system sends and receives short-range radio signals containing information on the load to tollbooths, weigh stations, and border

RFID tags can be attached to pallets of products or to individual items, such as clothing tags.

crossings. If the cargo meets requirements, the truck or train receives a green light to go ahead. Questionable cargo is set aside for further inspection. Transportation industry experts say the system can reduce delivery times by three hours or more.[18]

ADVANCED COMPUTER TECHNOLOGY

Advanced computer technology has boosted the efficiency of logistics dramatically with tools such as automatic identification systems (auto ID) using bar coding and radio-frequency technology, communications technology, and supply chain software systems that help synchronize the flow of goods and information with customer demand. Amazon.com's state-of-the-art distribution centers, for instance, use sophisticated order picking systems that utilize computer terminals to guide workers through the picking and packing process. Radio-frequency technology, which uses radio signals that work with scanned bar codes to identify products, directs Amazon's workers to the exact locations in the warehouse where the product is stored. Warehouse management software examines pick rates, location, and picking and storage patterns, and builds combinations of customer orders for shipping. After installing these supply chain technology tools, Amazon saw a 70 percent improvement in operational efficiency.

radio-frequency identification (RFID)
An automatic identification method that uses radio signals that work with scanned bar codes to identify products; data is stored in and retrieved from the RFID tag, which is attached to a product.

Procter & Gamble and many other companies use radio-frequency identification (RFID) tags in shipments to Wal-Mart stores. RFID tags are chips attached to a pallet of goods that allow the goods to be tracked from the time they are packed at the manufacturing plant until the consumer purchases them. Benefits include increased revenue for Wal-Mart (because the shelves are always full) and reduced inventory management costs (because overstocking and time spent counting items is minimized). Best Buy is currently planning to use an RFID-enabled payment system to reduce and eventually eliminate checkout lines at the front of the store—customers with a personalized Best Buy RFID shopping card could simply load up their carts and walk out the front door, with their checking or credit card account debited for the price of their merchandise before they even unlock their car.[19] However, RFID has been slower than expected in penetrating the retail sector; while 44 percent of manufacturers had adopted RFID at some level in early 2007, only 9 percent of retailers had done so.[20] Though some experts attribute the slowness of retail adoption of RFID to its complexity of implementation, many others suggest that retailers are scared away because of difficulty in determining their return on RFID-related investment.

One of the other major goals of technology is to bring up-to-date information to the supply chain manager's desk. The transportation system has long been referred to as an informational "black hole," where products and materials fall out of sight until they reappear some time later in a plant, store, or warehouse. Now carriers have systems that track freight, monitor the speed and location of carriers, and make routing decisions on the spur of the moment. Roadway Express, named one of the "Top 100 U.S. Motor Carriers" by Inbound Logistics, handles more than 70,000 shipments a day, many for large retailers like Wal-Mart, Target, and Home Depot. Information technology systems enable each package to be tracked from the minute it is received at one of Roadway's terminals until it is delivered. Customers can check on the progress of their shipment anytime by logging on to Roadway's Web site and entering the tracking number. Companies needing trucking services can go to the Inbound Logistics Web site and use their Trucking Decision Support Tool to identify motor carriers that can meet their service needs.[21] Swedish-based communications giant Ericsson, whose operations span the globe, uses specialized supply chain software to gain visibility over the 50,000 outbound shipments it makes a year. As products leave its manufacturing facilities, transportation providers transmit status information at specified intervals to Ericsson's information system, which is accessible to management using a standard Web browser. The company has benefited greatly from the increased visibility of shipments the system has provided. Ericsson's management is now in a position to identify bottlenecks and

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UPS offers more services than its hallmark package delivery. In fact, UPS helps companies open new global supply chains, manage raw material, and add distribution channels. To find out more, visit www.ups.com/supplychain.

respond before a crisis occurs, as well as measure the performance of its supply chain at different checkpoints.[22]

OUTSOURCING LOGISTICS FUNCTIONS

External partners are becoming increasingly important in the efficient deployment of supply chain management. Outsourcing, or contract logistics, is a rapidly growing segment of the distribution industry in which a manufacturer or supplier turns over an entire function of the logistics system, such as buying and managing transportation or warehousing, to an independent third party (3PL's, as mentioned earlier in the chapter). Many manufacturers are turning to outside partners for their logistics expertise in an effort to focus on the core competencies that they do best. Partners create and manage entire solutions for getting products where they need to be, when they need to be there. Logistics partners offer staff, an infrastructure, and services that reach consumers virtually anywhere in the world. Because a logistics provider is focused, clients receive service in a timely, efficient manner, thereby increasing customers' level of satisfaction and boosting their perception of added value to a company's offerings.

Third-party contract logistics allows companies to cut inventories, locate stock at fewer plants and distribution centers, and still provide the same or increased level of service. The companies then can refocus investment on their core business. Ford Motor Company uses third-party logistics provider UPS Worldwide Logistics Group to manage the delivery of Ford, Lincoln, and Mercury cars and trucks in the United States, Canada, and Mexico. The alliance between Ford and UPS has substantially reduced the time it takes to move vehicles from Ford's assembly plants to dealers and customers. Moreover, the Web-based system enables Ford and its dealers to track an individual vehicle's location from production through delivery to the final destination. Similarly, in the hospitality industry, procurement services company Avendra enables Fairmont Hotels & Resorts, Hyatt Hotels, Intercontinental Hotels Group, Marriott International, and others to enjoy significant savings and value-added supply chain services.[23] Avendra negotiates with suppliers to obtain virtually everything a hotel might need, from food and beverages to golf course maintenance. By relying on Avendra to manage many aspects of the supply chain, the hotels are able to concentrate on their core function—providing hospitality.

Many firms are taking outsourcing one step further by allowing business partners to take over the final assembly of their product or its packaging in an effort to reduce inventory costs, speed up delivery, or better meet customer requirements. Ryder Truck Lines assembles and packages 22 different combinations of shrink-wrapped boxes that contain the ice trays, drawers, shelves, doors, and other accessories for the various refrigerator models Whirlpool sells. Similarly, outsourcing firm StarTek, Inc., packages and ships products for Microsoft, provides technical support to customers of America Online, and maintains AT&T communication systems.[24]

outsourcing (contract logistics)
A manufacturer's or supplier's use of an independent third party to manage an entire function of the logistics system, such as transportation, warehousing, or order processing.

electronic distribution
A distribution technique that includes any kind of product or service that can be distributed electronically, whether over traditional forms such as fiber-optic cable or through satellite transmission of electronic signals.

ELECTRONIC DISTRIBUTION

Electronic distribution is the most recent development in the logistics arena. Broadly defined, electronic distribution includes any kind of product or service that can be distributed electronically, whether over traditional forms such as

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Electronic distribution has become a viable channel for many products, including tax preparation software, postage stamps, and even movie tickets, which can be purchased over the Internet prior to a show.

fiber-optic cable or through satellite transmission of electronic signals. For instance, instead of buying and installing software from stores, computer users purchase and download software over the Internet or rent the same software from Internet services that have the program available for use on their servers. For example, Intuit, Inc., allows people to fill out their tax returns on its Web site for a fee rather than buying its TurboTax software. Consumers can purchase tickets to sporting events, concerts, and movies over the Internet and print the tickets at home. And music, television shows, and movies have long been delivered to consumers through electronic pipelines. (Apple sold over 20 million songs and TV shows through iTunes in 2005 alone.)[25]

One of the most innovative electronic distribution ventures of late has come from ESPN. The sports broadcaster has leased high-speed network capacity from Sprint to create Mobile ESPN. Through a special cell phone, Mobile ESPN broadcasts a rich multimedia package unlike anything else. Its sports service includes news, scores, videos, alerts, fantasy teams, ESPN columnists, and more. There's also a special section where users can select to receive news and stats about their favorite players and teams.[26]

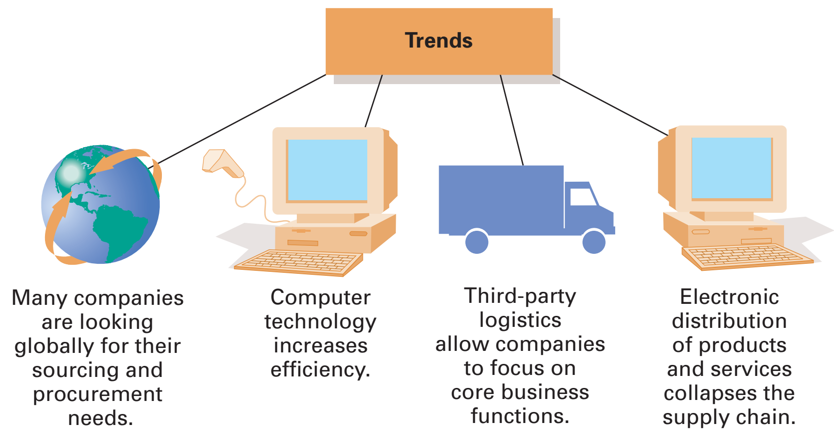
SUPPLY CHAIN SECURITY

Due to recent world events, firms are expending more effort on securing their supply chains from external threats than at any time in recent memory. Natural disasters, widespread technology failures, political instability, terrorism, disease pandemics, and worker strikes are but a few of the major events that can cause a supply chain to shut down temporarily or for an extended amount of time. The supply chain must be guarded from end to end because it is only as strong as its weakest link.

Managing supply chain disruptions begins with identifying the risks potentially affecting each node and link in the supply chain network.[27] This is especially true when the supply chain is global, with nodes and links located in or across international boundaries. Global supply chains are particularly at risk because members in far-away places often fail to completely understand the political, legal, and technological culture of the local area. Once risks are identified and assessed, the firm should put controls in place to monitor dangerous or volatile situations, and buy insurance when it appears that things could go wrong in the supply chain. The very best supply chains with respect to security also build contingency plans that are able to address situations quickly in the event of an emergency and get the supply chain back online. In fact, some businesses have completely replicated their systems and facilities in different geographic locations and, in the event of a disaster, can activate these backups within 24 hours.

REVIEW LEARNING OUTCOME

LO7 Discuss the new and emerging trends in supply chain management



9.5 < percentage of the U.S. gross domestic product generated by supply chain managers

U.S. IKEA suppliers > **1,600**

20 < percent reduction in inventory levels IKEA made with its new logistics management program

days required for GM to switch manufacturing facilities with its new flexible manufacturing system > **3**

6 < weeks required to make a similar transition with the old system

money GM saves yearly with the flexible manufacturing system > **$1.5 billion**

percentage of sales returned in apparel e-retailing > **40**

24 < hours within which the Marine Corps hopes to deliver supplies to the front lines

value of purchased goods imported to the U.S. > **$2 trillion**

150 < robots processing, collecting, and packing orders at Staples

Review and Applications

LO 1

Define supply chain and supply chain management and discuss their benefits. Supply chain management coordinates and integrates all of the activities performed by supply chain members into a seamless process from the source to the point of consumption. The responsibilities of a supply chain manager include developing channel design strategies, managing the relationships of supply chain members, sourcing and procurement of raw materials, scheduling production, processing orders, managing inventory and storing product, and selecting transportation modes. The supply chain manager is also responsible for managing customer service and the information that flows through the supply chain. The benefits of supply chain management include reduced costs in inventory management, transportation, warehousing, and packaging; improved service through techniques like time-based delivery and make-to-order; and enhanced revenues, which result from such supply chain-related achievements as higher product availability and more customized products.

1.1 Discuss the benefits of supply chain management. How does the implementation of supply chain management result in enhanced customer value?

LO 2

Discuss the concept of supply chain integration and explain why each of the six types of integration is important. Supply chain integration occurs when multiple firms in a supply chain coordinate their activities and processes so that they are seamlessly linked to one another in the attempt to satisfy customers. The six types of integration are as follows. (1) Relationship integration is the ability of two or more firms to develop tight social connections among their employees, resulting in smoother personal interactions. (2) Measurement integration is the idea that performance assessments should be transparent and similar across all of the supply chain members. (3) Technology and planning integration refers to the creation and maintenance of supply chain technology systems that connect managers throughout the supply chain. (4) Material and service supplier integration reflects a focus on integrating processes and functions with those who provide the company with the things they need in order to execute their core functions. (5) Internal operations integration is the development of capabilities for the firm's internal functional areas to communicate and work together on processes and projects. (6) Customer integration implies that firms evaluate their own capabilities and use them to offer long-lasting, distinctive, value-added offerings in ways that best serve their customers.

2.1 Discuss the concept of supply chain integration. How does it result in better customer-related outcomes?

2.2 What are some of the likely outcomes of a firm's failure to embrace one or more supply chain integration types?

LO 3

Identify the eight key processes of excellent supply chain management and discuss how each of these processes impacts the end customer. The key processes that leading supply chain companies focus on are (1) customer relationship management, (2) customer service management, (3) order fulfillment, (4) manufacturing flow management, (5) supplier relationship management,

(6) product development and commercialization, (7) returns management, and (8) demand management. When firms practice excellent supply chain management, each of these processes is integrated from end to end in the supply chain. These processes are made up of bundles of interconnected activities that supply chain partners are constantly focused on when delivering value to the customer.

3.1 What are the key processes in supply chain management, and who performs them? How does each process lead to increased satisfaction on the part of the customer?

LO4

Discuss the key strategic decisions supply chain managers must make when designing their companies' supply chains. Based on the firm's goals, the markets it competes in, and the availability of supply, firms will adopt a lean, agile, or combination (Leagile) strategy for supply chain management. Lean firms focus on improving profitability through the removal of waste from the supply chain system. Alternatively, agile firms are concerned primarily with customer responsiveness and service, and seek to provide the highest levels of responsiveness possible, even if the costs of doing so are higher. Leagile firms adopt a position somewhere between lean and agile, with main components made and shipped using lean principles, but with agility gained late in the process through the postponement of final production. Firms should also learn to map their supply chains so that they can understand the linkages between firms in the network that are all seeking to achieve the common goal of customer satisfaction.

4.1 When should firms pursue lean, agile, and/or Leagile supply chain strategies?

4.2 What are the expected benefits that may come from supply chain mapping?

LO5

Describe the logistical components of the supply chain. The logistics supply chain consists of several interrelated and integrated logistical components: (1) sourcing and procurement of raw materials and supplies, (2) production scheduling, (3) order processing, (4) inventory control, (5) warehousing and materials-handling, and (6) transportation. The logistics information system is the link connecting all of the logistics components of the supply chain. Information technology connects the various components and partners of the supply chain into an integrated whole. The supply chain team, in concert with the logistics information system, orchestrates the movement of goods, services, and information from the source to the consumer. Supply chain teams typically cut across organizational boundaries, embracing all parties who participate in moving product to market. Procurement deals with the purchase of raw materials, supplies, and components according to production scheduling. Order processing monitors the flow of goods and information (order entry and order handling). Inventory control systems regulate when and how much to buy (order timing and order quantity). Warehousing provides storage of goods until needed by the customer while the materials-handling system moves inventory into, within, and out of the warehouse. Finally, the major modes of transportation are railroads, motor carriers, pipelines, waterways, and airways.

5.1 Discuss the impact of build-to-order production on the entire supply chain. Specifically, how does build-to-order manufacturing affect suppliers, procurement planning, inventory levels, mode of transportation selected, and warehousing? What are the benefits of build-to-order manufacturing to the end consumer?

5.2 Assume that you are the supply chain manager for a producer of expensive, high-tech computer components. Identify the most suitable method(s) of transporting your product in terms of cost, transit time, reliability, capability, accessibility, and traceability. Now, assume you are the supply chain manager for a producer of milk. How does this change your choice of transportation?

LO6

Explain why supply chain performance measurement is necessary and important. Because supply chains are often very complex, with each firm in the chain seeking to fulfill its own goals, it is sometimes difficult to determine whether the supply chain as a whole is functioning well. Firms in the best supply chains develop and use common metrics to assess whether customers are satisfied and whether operations are completed in a timely fashion, at an acceptable level of cost, and with good asset utilization. Often, this includes the use of the Balanced Scorecard methodology, which assures that not only will customers be satisfied, but also that the firm will execute its tasks with process efficiency, with financially acceptable returns, and in a way that allows for learning and growth for the company.

6.1 Why is supply chain performance measurement necessary and important?

6.2 How does the Balanced Scorecard Approach help firms within the supply chain to establish and meet common goals?

LO7

Discuss new technology and emerging trends in supply chain management. Several emerging trends are changing the job of today's supply chain manager. Technology and automation are bringing up-to-date distribution information to the decision maker's desk. Technology is also linking suppliers, buyers, and carriers for joint decision making, and it has created a new electronic distribution channel. Many companies are saving money and time by outsourcing third-party carriers to handle some or all aspects of the distribution process. Firms are taking major steps toward the goal of securing their supply chains from external threats.

ONLINE

7.1 Visit the Web site of Menlo Logistics at http://www.menlolog.com. What logistics functions can this third-party logistics supplier provide? How does its mission fit in with the supply chain management philosophy?

Key Terms

ABC segmentation	410
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agile supply chain management	418
automatic replenishment programs	424
Balanced Scorecard Approach	427
benchmarks	410
business process	411
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Exercises

APPLICATION EXERCISE

From your readings, you might feel that you have a general idea as to how supply chain management works. However, in reality, the practice of supply chain management can be very complicated. This exercise will help you to identify the complexities of managing a global supply chain in a real world setting. By following one of your favorite products as its many components migrate through the supply chain on their long road to your home or office, you may gain additional appreciation for the difficult tasks supply chain managers face daily.

Activities

1. Pick a product with which you are very familiar or that you anticipate being able to research easily. You may want to consult family members, relatives, or even a former or current employer who can give you details of the business.

2. Map the supply chain of your product as far back as is feasible. A simple example is a diamond sold by a local jewelry store, purchased direct from diamond wholesalers in the Netherlands, bought by wholesalers from diamond centers in South Africa, brought out of mines owned by a company in South Africa. Identify as many participants in the channel as possible by company name and location.
3. Identify the mode of transportation used between each stage in the channel.
4. Identify by name and location the component parts of the product, if any. For example, let's expand the diamond example from a single diamond to a diamond necklace. You would need to trace the history of both the metal chain and the diamond back to their origins and forward until the point at which the diamond and chain are combined to form the diamond necklace.

ETHICS EXERCISE

For years, labor and environmental groups have criticized and pressured companies whose suppliers pay low wages, run sweatshops, use child labor, or use other similarly illicit labor practices. However, only recently have U.S. companies begun to come under fire for sourcing materials from foreign companies who are contributing to massive pollution problems in their local environments. When it was discovered that the Fuan Textiles plant in southern China, a major fabric supplier for companies such as Nike, Liz Claiborne, and Target, had been dumping large quantities of untreated waste water into Chinese lakes and rivers, many U.S. companies downstream in the Fuan supply chain were forced to take notice. As Daryl Brown, VP for Ethics and Compliance at Liz Claiborne noted, "The environment is the new frontier. We certainly don't want to be associated with a company that's polluting the waters." [28]

Questions

1. Should companies such as Nike, Liz Claiborne, and Target avoid structuring their supply chains so that they include polluters, even if the pollution is occurring somewhere far from the United States?
2. What are the pros and cons associated with using supplies and/or labor sourced from supply chain partners (direct and indirect) based in countries that do not have strict pollution standards?
3. Does the AMA Statement of Ethics address the issue of environmental protection in supply chain management? Go to **http://www.marketingpower.com** and review the code. Then, write a business memo to the Liz Claiborne president that describes how the AMA Statement of Ethics addresses the dilemma faced by the company.

Case Study: Dell

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CAN THE ICON OF THE LOGISTICS INDUSTRY SUCCEED IN INDIA? [29]

Michael Dell had the idea of selling computer systems directly to customers when he was a student at the University of Texas. In 1985 his new company designed its first computer system and soon began offering next-day, onsite product service. By 1996 Dell was selling computers on the Internet, and by 2000 the company's Web site was pulling in $50 million a day in direct sales.

Today Dell is well established as an icon of the logistics industry. Its lean business model has influenced countless other companies to follow its lead. Dell's 300,000 square-foot Morton L. Topfer Manufacturing Center (known as TMC) in Texas serves as ground zero for the build-to-order (or "just-in-time") manufacturing processes it's famous for. The TMC makes it possible for Dell to assemble hundreds of computers an hour, taking orders as they come in and making them to the customers' specifications. In the computer industry, technological equipment quickly becomes outdated, so Dell wants everything that goes out the door to be fresh off the assembly line—not losing value in a warehouse.

Dell's revolutionary supply chain is characterized by its minimum levels of inventory, a policy of paying suppliers only after the customers have paid Dell, and direct sales. Industry analysts say that these strategies have changed high-tech manufacturing the way Wal-Mart changed retail.

The question for Dell now is how to plan for future growth in emerging global markets such as China and India. Can Dell's business model, which is based on information, efficiency, and speed, work as well in parts of the world where the economic and social contexts are so different from how they are in the U.S.?

Dell announced plans for major capital investment and expansion in its Indian operations that calls for 20,000 employees and a new manufacturing facility similar to TMC by 2009. Analysts predict that if Dell is successful in bringing its JIT implementation to India, it could spur a movement of manufacturing-focused foreign investment in the country.

A 2005 report by KPMG International concluded that China and India will be the world's two biggest economies by mid-century, and, "although India has underperformed in the last lap of the growth race, there is a strong possibility that India may well move ahead." Dell appears to agree. CEO Kevin Rollins explained: "India currently sells 4 million computers per year and this is projected to rise to 10 million units annually in the next three to five years. Our workforce here is capable and the time is right for the second phase of expansion in contact center activities, research and development and . . . a manufacturing site."

Critics are skeptical that India will be as profitable as Dell hopes, however, citing the country's lack of reliable roads, power, and telecommunications. Although telecommunications have improved with a 53,000-mile fiber-optic network, India maintains only 2,000 miles of highways (the U.S. has 23 times that). Delivery chains rely almost exclusively on small vehicles with only three wheels that navigate on dirt roads. As for India's power supply, business owners experience nearly 20 significant outages every month (compared to 5 in China). Add to this the hassle of endless red tape required of businesses in India, labor regulations that force businesses to get government permission to lay off workers, and laws that require unanimous worker approval before companies can reorganize, and it becomes clear why critics wonder whether Dell can succeed there.

Dell counters that their computers are lightweight enough to be transported in the three-wheeled trucks that are the backbone of the Indian supply chain. And industry observer Clay Risen adds, "Dell's requirement that suppliers locate warehouses nearby suddenly seems an advantage—after all, the less the supply chain has to deal with the Indian transportation system, the better." Dell can concentrate on the urban middle class with the money to buy computers in major cities like New Delhi, where the country's infrastructure, power, and telecommunications systems are more reliable.

Even with the risks involved with doing business there, Dell has decided that India is too large and full of possibilities to ignore. The industry is watching and waiting to see how the computer giant fares. Dell's success—or failure—could determine whether more manufacturing companies follow its example in the future.

Questions

1. Describe how Dell's manufacturing processes represent a change in chain management from how things were done during the mass-production era. What does it mean that there has been a reversal of the flow of demand from a "push" to a "pull" system?
2. Describe the order processing system. How does it work in a company like Dell? As an order enters the system, what must management monitor? Why is it so important that the order processing system be executed well?
3. Describe the role that a supply chain manager at Dell might play. What would his or her responsibilities be? Why is there such high demand for supply chain managers in companies like Dell today?
4. Describe the benefits that Dell and other companies receive from supply chain management. What benefits do supply-chain oriented companies commonly report? What has research shown?

Company Clips

SEPHORA—BUSINESS IS BEAUTIFUL—PART 2

As you saw in the video for chapter 13, Sephora is a leader in sales of heath and beauty-aid products. Its shelves are stocked with a balance of big brand names and lesser known, up-and-coming brands. Sephora also carries and promotes its own private brand. With such an extensive, expanding, and ever-freshened inventory, Sephora must maintain an efficient supply chain—one that handles sourcing and procurement of raw supplies for the Sephora brand, production scheduling, order processing, inventory control, warehousing, materials handling, and transportation. Review the Company Clip from chapter 13 to learn what supply-chain techniques Sephora uses to keep its shelves stocked and customers happy.

Questions

1. Why is important to customers that Sephora keep detailed information about its inventory? What does Sephora do to insure its numbers are accurate?
2. How does Sephora manage its supply chain? What information goes into deciding which suppliers become incorporated?

Marketing & You Results

The higher your score, the more you are committed to providing quality services to your customers. A high score also suggests that your boss was committed to service quality, empowered you to make decisions, and that you were satisfied with your job. As you learned in this chapter, when everyone working within the company is "on the same page," the company can better provide a seamless and satisfying customer experience.

Retailing

CHAPTER 15

Learning Outcomes

LO 1 Discuss the importance of retailing in the U.S. economy
LO 2 Explain the dimensions by which retailers can be classified
LO 3 Describe the major types of retail operations
LO 4 Discuss nonstore retailing techniques
LO 5 Define franchising and describe its two basic forms
LO 6 List the major tasks involved in developing a retail marketing strategy
LO 7 Describe new developments in retailing

LO 1
The Role of Retailing

retailing
All the activities directly related to the sale of goods and services to the ultimate consumer for personal, nonbusiness use.

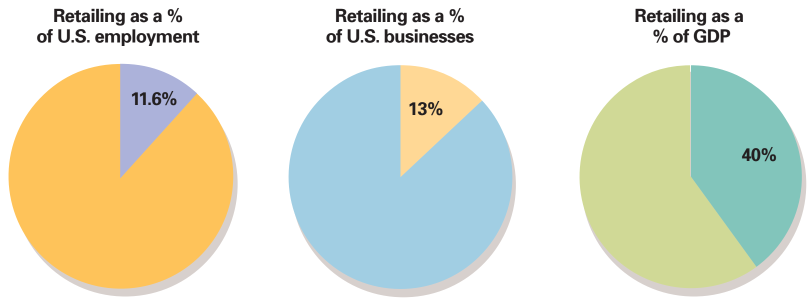
Retailing—all the activities directly related to the sale of goods and services to the ultimate consumer for personal, nonbusiness use—has enhanced the quality of our daily lives. When we shop for groceries, hair styling, clothes, books, and many other products and services, we are involved in retailing. The millions of goods and services provided by retailers mirror the needs and styles of U.S. society.

Retailing affects all of us directly or indirectly. The retailing industry is one of the largest employers; over 1.6 million U.S. retailers employ more than 24 million people—about one in five American workers.[1] Retail trade accounts for 11.6 percent of all U.S. employment, and almost 13 percent of all businesses are considered retail under NAICS. At the store level, retailing is still largely a mom-and-pop business. Almost nine out of ten retail companies employ fewer than 20 employees, and, according to the National Retail Federation, over 90 percent of all retailers operate just one store.[2]

The U.S. economy is heavily dependent on retailing. Retailers ring up over $4 trillion in sales annually, about 40 percent of the gross domestic product (GDP).[3] Although most retailers are quite small, a few giant organizations dominate the industry, most notably Wal-Mart, whose annual U.S. sales alone are greater than the next five U.S. retail giants' sales combined. Who are these giants? Exhibit 15.1 lists the ten largest U.S. retailers.

REVIEW LEARNING OUTCOME

LO 1 Discuss the importance of retailing in the U.S. economy



Marketing & You

How much do you enjoy shopping? Enter your answers on the lines provided.

1	2	3	4	5	6
Strongly disagree	Disagree	Neutral	Agree	Strongly agree

— I shop because buying things makes me happy.

— Shopping is fun.

— I get a real "high" from shopping.

— I enjoy talking with salespeople and other shoppers who are interested in the same things I am.

— I like having a salesperson bring merchandise out for me to choose from.

— I enjoy seeing mall exhibits while shopping.

Total your score, and find out what it means after you read the chapter.

LO 2
Classification of Retail Operations

A retail establishment can be classified according to its ownership, level of service, product assortment, and price. Specifically, retailers use the latter three variables to position themselves in the competitive marketplace. (As noted in Chapter 8, positioning is the strategy used to influence how consumers perceive one product in relation to all competing products.) These three variables

Exhibit 15.1

Ten Largest U.S. Retailers

2006 Rank	Company	Retailing Formats	2006 Revenue (billions)	2006 Number of Stores
1	**Wal-Mart** Bentonville, AR	Discount stores, supercenters, and warehouse clubs	348.7	6,779
2	**Home Depot** Atlanta, GA	Home centers	90.8	2,147
3	**Kroger** Cincinnati, OH	Supermarkets and convenience stores	66.1	3,659
4	**Costco** Issaquah, WA	Warehouse clubs	60.2	488
5	**Target** Minneapolis, MN	Discount stores and supercenters	59.5	1,487
6	**Sears Holding** Hoffman Estates, IL	Department stores, catalogs, home centers, and specialty	53.0	3,835
7	**Walgreens** Deerfield, IL	Drugstores	47.4	5,461
8	**Lowe's** Mooresville, NC	Home centers	46.9	1,375
9	**CVS** Woonsocket, RI	Drugstores	43.8	6,202
10	**Safeway** Pleasanton, CA	Supermarkets	40.2	1,761

SOURCE: STORES, July 2007, **http://www.stores.org.** Sales figures include international sales.

Exhibit 15.2

Types of Stores and Their Characteristics

Type of Retailer	Level of Service	Product Assortment	Price	Gross Margin
Department store	Moderately high to high	Broad	Moderate to high	Moderately high
Specialty store	High	Narrow	Moderate to high	High
Supermarket	Low	Broad	Moderate	Low
Convenience store	Low	Medium to narrow	Moderately high	Moderately high
Drugstore	Low to moderate	Medium	Moderate	Low
Full-line discount store	Moderate to low	Medium to broad	Moderately low	Moderately low
Discount specialty store	Moderate to low	Medium to broad	Moderately low to low	Moderately low
Warehouse clubs	Low	Broad	Low to very low	Low
Off-price retailer	Low	Medium to narrow	Low	Low
Restaurant	Low to high	Narrow	Low to high	Low to high

can be combined in several ways to create distinctly different retail operations. Exhibit 15.2 lists the major types of retail stores discussed in this chapter and classifies them by level of service, product assortment, price, and gross margin.

OWNERSHIP

Retailers can be broadly classified by form of ownership: independent, part of a chain, or franchise outlet. Retailers owned by a single person or partnership and not operated as part of a larger retail institution are independent retailers. Around the world, most retailers are independent, operating one or a few stores in their community. Local florists, shoe stores, and ethnic food markets typically fit this classification.

Chain stores are owned and operated as a group by a single organization. Under this form of ownership, many administrative tasks are handled by the home office for the entire chain. The home office also buys most of the merchandise sold in the stores. Gap and Starbucks are examples of chains.

Franchises are owned and operated by individuals but are licensed by a larger supporting organization, such as Subway or Quiznos. The franchising approach combines the advantages of independent ownership with those of the chain store organization. Franchising is discussed in more detail later in the chapter.

LEVEL OF SERVICE

The level of service that retailers provide can be classified along a continuum, from full service to self-service. Some retailers, such as exclusive clothing stores, offer high levels of service. They provide alterations, credit, delivery, consulting, liberal return policies, layaway, gift wrapping, and personal shopping. Discount stores usually offer fewer services. Retailers like factory outlets and warehouse clubs offer virtually no services.

PRODUCT ASSORTMENT

The third basis for positioning or classifying stores is by the breadth and depth of their product line. Specialty stores—for example, Best Buy, Toys "R" Us, or GameStop—have the most concentrated product assortments, usually carrying single or narrow product lines but in considerable depth. On the other end of the spectrum, full-line discounters typically carry broad assortments of merchandise with limited depth. For example, Target carries automotive supplies, household cleaning products, and pet food. Typically, though, it carries only four or five brands of dog food. In contrast, a specialty pet store, such as Petsmart, may carry as many as 20 brands in a large variety of flavors, shapes, and sizes.

Other retailers, such as factory outlet stores, may carry only part of a single line. Nike stores sell only certain items of its own brand. Discount specialty stores like Home Depot and Rack Room Shoes carry a broad assortment in concentrated product lines, such as building and home supplies or shoes.

independent retailers
Retailers owned by a single person or partnership and not operated as part of a larger retail institution.

chain stores
Stores owned and operated as a group by a single organization.

franchise
The right to operate a business or to sell a product.

gross margin
The amount of money the retailer makes as a percentage of sales after the cost of goods sold is subtracted.

department store
A store housing several departments under one roof.

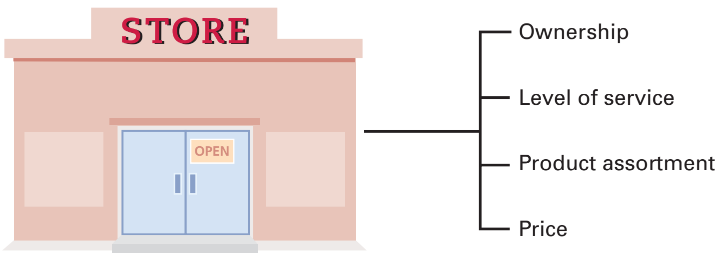
PRICE

Price is a fourth way to position retail stores. Traditional department stores and specialty stores typically charge the full "suggested retail price." In contrast, discounters, factory outlets, and off-price retailers use low prices as a major lure for shoppers.

The last column in Exhibit 15.2 shows the typical gross margin—how much the retailer makes as a percentage of sales after the cost of goods sold is subtracted. The level of gross margin and the price level generally match. For example, a traditional jewelry store has high prices and high gross margins. A factory outlet has low prices and low gross margins. Markdowns on merchandise during sale periods and price wars among competitors, in which stores lower prices on certain items in an effort to win customers, cause gross margins to decline. When Wal-Mart entered the grocery business in a small Arkansas community, a fierce price war ensued. By the time the price war was in full swing, the price of a quart of milk had plummeted by more than 50 percent (below the price of a pint) and a loaf of bread sold for only 9 cents—prices at which no retailer could make a profit.

REVIEW LEARNING OUTCOME

LO 2 Explain the dimensions by which retailers can be classified



LO 3 Major Types of Retail Operations

Traditionally, there have been several distinct types of retail stores, each offering a different product assortment, type of service, and price level, according to its customers' shopping preferences.

In a recent trend, however, retailers are experimenting with alternative formats that make it harder to classify them. For instance, supermarkets are expanding their nonfood items and services; discounters are adding groceries; drugstores are becoming more like convenience stores; and department stores are experimenting with smaller stores. Nevertheless, many stores still fall into the basic types.

DEPARTMENT STORES

A department store carries a wide variety of shopping and specialty goods, including apparel, cosmetics, housewares, electronics, and sometimes furniture. Purchases are generally made within each department rather than at one central checkout area. Each department is treated as a separate buying center to achieve economies in promotion, buying, service, and control. Each department is usually

buyer
A department head who selects the merchandise for his or her department and may also be responsible for promotion and personnel.

specialty store
A retail store specializing in a given type of merchandise.

supermarket
A large, departmentalized, self-service retailer that specializes in food and some nonfood items.

headed by a buyer, a department head who not only selects the merchandise for his or her department but may also be responsible for promotion and personnel. For a consistent, uniform store image, central management sets broad policies about the types of merchandise carried and price ranges. Central management is also responsible for the overall advertising program, credit policies, store expansion, customer service, and so on.

Large independent department stores are rare today. Most are owned by national chains. Among the largest U.S. department store chains are Macy's, Inc. (formerly known as Federated Department Stores, Inc.), JCPenney, Sears, Dillard's, and Nordstrom. Dillard's is known for its distribution expertise. Nordstrom offers innovative customer service.

SPECIALTY STORES

Specialty store formats allow retailers to refine their segmentation strategies and tailor their merchandise to specific target markets. A specialty store is not only a type of store but also a method of retail operations—namely, specializing in a given type of merchandise. Examples include children's clothing, men's clothing, candy, baked goods, gourmet coffee, sporting goods, and pet supplies. A typical specialty store carries a deeper but narrower assortment of specialty merchandise than does a department store. Generally, specialty stores' knowledgeable sales clerks offer more attentive customer service. The format has become very powerful in the apparel market and other areas. In fact, consumers buy more clothing from specialty stores than from any other type of retailer. The Children's Place, Gadzooks, Williams-Sonoma, and Foot Locker are examples of successful chain specialty retailers.

Consumers usually consider price to be secondary in specialty outlets. Instead, the distinctive merchandise, the store's physical appearance, and the caliber of the staff determine its popularity. For example, industry experts found that consumers are mostly confused by the wide array of new high-tech products available these days. One study found that only about 10 percent of the capability of new gadgetry is ever utilized.[4] Customers who shop for high-end electronics often find that specialty stores cannot compete on price with big-box stores. Instead, consumer electronics specialty stores compete by offering better-trained sales staff, more expertise, and better customer service than the big-box retailers. For instance, Tweeter, a regional electronics chain in New England, specializes in helping its customers overcome confusion and become comfortable with their purchases. Tweeter's customers can try out the latest technology by accompanying "hyper-informed" salespeople through replica kitchens, dens, and bedrooms loaded with complicated gadgets.[5] Because of their attention to the customer and limited product line, manufacturers often favor introducing new products in small specialty stores before moving on to larger retail and department stores.

SUPERMARKETS

According to the U.S. Department of Agriculture, U.S. consumers spend about 10 percent of their disposable income on food, and roughly half of those expenditures occur in supermarkets on food for at-home consumption. Supermarkets are large, departmentalized, self-service retailers that specialize in food and some nonfood items. Supermarkets have experienced declining sales in recent years. Some of this decline has been the result of increased competition from discounter Wal-Mart and Sam's Clubs. But demographic and lifestyle changes have also affected the supermarket industry.

One major change has been the increase in dual-income and single-parent families that eat out more or are just too busy to prepare meals at home. According to the U.S. Department of Agriculture, Americans spend about 50 percent of their food money in retail grocery stores, and nearly 50 percent on food away from home. In comparison, Americans spent over three-fourths of their food money in grocery stores in 1950.[6]

© AP PHOTO/MIKE GROLL

A new trend in supermarket diversification—or scrambled merchandising—is the addition of store-owned gas stations. The gas stations are not only a revenue source for the supermarkets, but they also attract customers to the location by offering lower prices than can usually be found at a traditional gas station.

As stores seek to meet consumer demand for one-stop shopping, conventional supermarkets are being replaced by bigger *superstores,* which are usually twice the size of supermarkets. Superstores meet the needs of today's customers for convenience, variety, and service. Superstores offer one-stop shopping for many food and nonfood needs, as well as many services—including pharmacies, flower shops, salad bars, in-store bakeries, takeout food sections, sit-down restaurants, health food sections, video rentals, dry-cleaning services, shoe repair, photo processing, and banking. Some even offer family dentistry or optical shops. This tendency to offer a wide variety of nontraditional goods and services under one roof is called scrambled merchandising. Safeway supermarkets are a good example of scrambled merchandising. In addition to including a liquor store, floral department, and pharmacy, they also lease space to Starbucks and local banks. Another trend in supermarket diversification is the addition of store-owned gas stations. The gas stations are not only a revenue source for the supermarkets and a convenience for customers, but they also attract customers to the location by offering lower prices than can usually be found at a traditional gas station. Store-owned stations are expected to account for as much as 20 percent of overall gasoline sales in the near future.

scrambled merchandising
The tendency to offer a wide variety of nontraditional goods and services under one roof.

drugstore
A retail store that stocks pharmacy-related products and services as its main draw.

To stand out in an increasingly competitive marketplace, many supermarket chains are tailoring marketing strategies to appeal to specific consumer segments. Most notable is the shift toward *loyalty marketing programs* that reward loyal customers carrying frequent shopper cards with discounts or gifts. Once scanned at the checkout, frequent shopper cards help supermarket retailers electronically track shoppers' buying habits. More than half of the customers who shop at the over 600 Piggly Wiggly stores carry the Pig's Favorite loyalty card. Customers use their card each time they shop to get special discounts on items. The supermarket chain was also one of the first grocers to implement biometrics. Instead of carrying a loyalty card, the customer simply places a fingertip on a biometric finger-scan reader at a kiosk positioned near the front of the store. The shopper then receives a printout of personalized offers, which change weekly.[7] Piggly Wiggly also uses consumer purchase data stored in its database to determine customer preferences. If management sees that a customer buys flowers regularly, then it sends that customer a coupon redeemable in its floral department.[8]

DRUGSTORES

Drugstores stock pharmacy-related products and services as their main draw. Consumers are most often attracted to a drugstore by its pharmacy or pharmacist, its convenience, or because it honors their third-party prescription drug plan. Drugstores also carry an extensive selection of over-the-counter (OTC) medications, cosmetics, health and beauty aids, seasonal merchandise, specialty items such as greeting cards and a limited selection of toys, and some nonrefrigerated convenience foods. As competition has increased from mass merchandisers and supermarkets with their own pharmacies, as well as from direct-mail prescription services, drugstores have added value-added services such as 24-hour operations, drive-through pharmacies, and low-cost health clinics staffed by nurse practitioners.

Demographic trends in the United States look favorable for the drugstore industry. As the baby boom population continues to age, they will spend an increasing percentage of their disposable income on health care and wellness. In fact, the average 60-year-old purchases 15 prescriptions per year, nearly twice as many as the average 30-year-old. Because baby boomers are attentive to their health and keenly sensitive about their looks, the increased traffic at the pharmacy counter in the future should also spur sales in other traditionally strong drugstore merchandise categories, most notably OTC drugs, vitamins, and health and beauty aids.

CONVENIENCE STORES

convenience store
A miniature supermarket, carrying only a limited line of high-turnover convenience goods.

discount store
A retailer that competes on the basis of low prices, high turnover, and high volume.

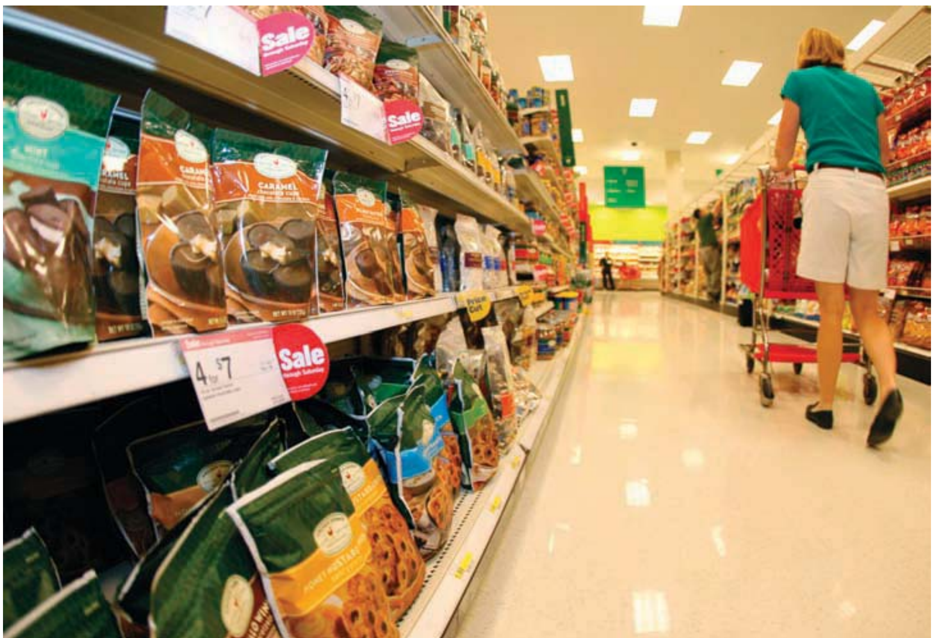
full-line discount stores
A retailer that offers consumers very limited service and carries a broad assortment of well-known, nationally branded "hard goods."

A convenience store can be defined as a miniature supermarket, carrying only a limited line of high-turnover convenience goods. These self-service stores are typically located near residential areas and are open 24 hours, seven days a week. Convenience stores offer exactly what their name implies: convenient location, long hours, and fast service. However, prices are almost always higher at a convenience store than at a supermarket. Thus, the customer pays for the convenience.

When the original convenience stores added self-service gas pumps, full-service gas stations fought back by closing service bays and opening miniature stores of their own, selling convenience items like cigarettes, sodas, and snacks. Supermarkets and discount stores also wooed customers with one-stop shopping and quick checkout. To combat the gas stations' and supermarkets' competition, convenience store operators have changed their strategy. They have expanded their offerings of nonfood items with video rentals and health and beauty aids and added upscale sandwich and salad lines and more fresh produce. Some convenience stores are even selling Pizza Hut, Subway, and Taco Bell products prepared in the store. For example, Exxon On the Run features Green Mountain Coffee Roasters, BLIMPIE subs and salads, and an On the Run Café that offers everything from fresh sandwiches and fresh fruits to a grilled hamburger and french fries.[9]

DISCOUNT STORES

A discount store is a retailer that competes on the basis of low prices, high turnover, and high volume. Discounters can be classified into four major categories: full-line discount stores, specialty discount stores, warehouse clubs, and off-price discount retailers.



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For supercenter operators such as Target, food is a customer magnet that sharply increases the store's overall volume, while taking customers away from traditional supermarkets.

Full-Line Discount Stores

Compared to traditional department stores, full-line discount stores offer consumers very limited service and carry a much broader assortment of well-known, nationally branded "hard goods," including housewares, toys, automotive parts, hardware, sporting goods, and

mass merchandising
A retailing strategy using moderate to low prices on large quantities of merchandise and lower service to stimulate high turnover of products.

supercenter
A retail store that combines groceries and general merchandise goods with a wide range of services.

garden items, as well as clothing, bedding, and linens. Some even carry limited nonperishable food items, such as soft drinks, canned goods, and potato chips. As with department stores, national chains dominate the discounters. Full-line discounters are often called mass merchandisers. Mass merchandising is the retailing strategy whereby retailers use moderate to low prices on large quantities of merchandise and lower service to stimulate high turnover of products.

Wal-Mart is the largest full-line discount store in terms of sales. Wal-Mart initially expanded rapidly by locating on the outskirts of small towns and absorbing business for miles around. In recent years, most of its growth has come in larger cities. Today, it has over 6,000 stores on four continents. Much of Wal-Mart's success has been attributed to its merchandising foresight, cost consciousness, efficient communication and distribution systems, and involved, motivated employees. Wal-Mart is credited with pioneering the retail strategy of "everyday low pricing," a strategy now widely copied by retailers the world over. Besides expanding throughout all 50 states and Puerto Rico, Wal-Mart has expanded globally into Argentina, Brazil, Canada, China, Costa Rica, El Salvador, Guatemala, Honduras, Japan, Mexico, Nicaragua, South Korea, and the United Kingdom. Wal-Mart has also become a formidable retailing giant in online shopping, concentrating on toys and electronics. With tie-ins to its stores across the country, Wal-Mart offers online shopping with in-store kiosks linking to the site and the ability to handle returns and exchanges from Internet sales at its physical stores.[10]

Supercenters combine a full line of groceries and general merchandise with a wide range of services, including pharmacy, dry cleaning, portrait studios, photo finishing, hair salons, optical shops, and restaurants—all in one location. For supercenter operators like Wal-Mart, food is a customer magnet that sharply increases the store's overall volume, while taking customers away from traditional supermarkets. Wal-Mart opened its first supercenter in 1988 and now operates over 2,000 supercenters worldwide. Target was the last major discounter to embrace the supercenter concept. The chain currently has 177 SuperTarget locations and plans to open 200 more over the next ten years[11]

Supercenters are also threatening to push Europe's traditional small and medium-sized food stores into extinction. Old-fashioned corner stores and family businesses are giving way to larger chains that offer food, drugs, services, and general merchandise all in one place. Today, the largest British food retailer is Tesco, a chain operator that has over 30 percent of the grocery market in the United Kingdom. Tesco is expanding rapidly and now has over 1,800 stores in the UK and almost 2,500 stores globally, including a joint venture with Safeway in the United States.[12]

Many European countries, however, are passing legislation to make it more difficult for supercenters to open. In France, for example, laws ban authorizations for new supercenters over 1,000 square meters (10,800 square feet). Belgium and Portugal have passed similar bans. In Britain and the Netherlands, areas outside towns and cities are off limits to superstores. By imposing planning and building restrictions for large stores, these countries are trying to accommodate environmental concerns, movements to revive city centers, and the worries of small shopkeepers.

An increasingly popular variation of full-line discount stores is *extreme-value retailing,* the most notable examples being Dollar General and Family Dollar. Extreme-value retailers have grown in popularity as major discounters continue to shift toward the supercenter format, broadening their customer base and increasing their offerings of higher-priced goods aimed at higher-income consumers. This has created an opening for extreme-value retailers to entice shoppers from the low-income segment. Low- and fixed-income customers are drawn to extreme-value retailers, whose stores are located within their communities. Extreme-value retailers also build smaller stores (a typical store is about the size of one department in a Wal-Mart superstore) with a narrower selection of merchandise emphasizing day-to-day necessities. Rock-bottom prices are also key to their success. With the average transaction under $10, extreme-value retailers have found low price to be far more critical to building traffic and loyalty than any other retailing format.[13]

Specialty Discount Stores

Another discount niche includes the single-line **specialty discount stores**—for example, stores selling sporting goods, electronics, auto parts, office supplies, housewares, or toys. These stores offer a nearly complete selection of single-line merchandise and use self-service, discount prices, high volume, and high turnover to their advantage. Specialty discount stores are often termed **category killers** because they so heavily dominate their narrow merchandise segment. Examples include Toys "R" Us in toys (the first category killer in the market), Circuit City and Best Buy in electronics, Staples and Office Depot in office supplies, Home Depot and Lowe's in home improvement supplies, IKEA in home furnishings, Bed, Bath & Beyond in kitchen and bath accessories, and Dick's in sporting goods.

Category killers have emerged in other specialty segments as well, creating retailing empires in highly fragmented mom-and-pop markets. For instance, the home improvement industry, which for years was served by professional builders and small hardware stores, is now dominated by Home Depot and Lowe's. Category-dominant retailers like these serve their customers by offering a large selection of merchandise, stores that make shopping easy, and low prices every day, which eliminates the need for time-consuming comparison shopping.

AP PHOTO/DOUGLAS C. PIZAC

Warehouse Membership Clubs

Warehouse membership clubs sell a limited selection of brand-name appliances, household items, and groceries. These are usually sold in bulk from warehouse outlets on a cash-and-carry basis to members only. Individual members of warehouse clubs are charged low or no membership fees. Currently, the leading stores in this category are Wal-Mart's Sam's Club, Costco, and BJ's Wholesale Club.

Warehouse clubs have had a major impact on supermarkets. With 90,000 square feet or more, warehouse clubs offer 60 to 70 percent general merchandise and health- and beauty-care products, with grocery-related items making up the difference. Warehouse club members tend to be more educated and more affluent and have a larger household than regular supermarket shoppers. These core customers use warehouse clubs to stock up on staples; then they go to specialty outlets or food stores for perishables. Warehouse clubs are also expanding into luxury items. In 2007, Sam's Club had a $347,000 diamond solitaire ring on sale before Christmas; Costco sells Dom Perignon champagne.

Off-Price Retailers

An **off-price retailer** sells at prices 25 percent or more below traditional department store prices because it pays cash for its stock and usually doesn't ask for return privileges. Off-price retailers buy manufacturers' overruns at cost or even less. They also absorb goods from bankrupt stores, irregular merchandise, and unsold end-of-season output. Nevertheless, much off-price retailer merchandise is first-quality, current goods. Because buyers for off-price retailers purchase only what is available or what they can get a good deal on, merchandise styles and brands often change monthly. Today, there are hundreds of off-price retailers, including T. J. Maxx, Ross Stores, Marshall's, HomeGoods, and Tuesday Morning.

Factory outlets are an interesting variation on the off-price concept. A **factory outlet** is an off-price retailer that is owned and operated by a manufacturer. Thus, it carries one line of merchandise—its own. Each season, from 5 to 10 percent of a manufacturer's output does not sell through regular distribution channels because it consists of closeouts (merchandise being discontinued), factory seconds, and canceled orders. With factory outlets, manufacturers can regulate where their surplus is sold, and they can realize higher profit margins than they would by disposing of

specialty discount store
A retail store that offers a nearly complete selection of single-line merchandise and uses self-service, discount prices, high volume, and high turnover.

category killers
Specialty discount stores that heavily dominate their narrow merchandise segment.

warehouse membership clubs
Limited-service merchant wholesalers that sell a limited selection of brand-name appliances, household items, and groceries on a cash-and-carry basis to members, usually small businesses and groups.

off-price retailer
A retailer that sells at prices 25 percent or more below traditional department store prices because it pays cash for its stock and usually doesn't ask for return privileges.

factory outlet
An off-price retailer that is owned and operated by a manufacturer.

the goods through independent wholesalers and retailers. Factory outlet malls are typically located in out-of-the-way rural areas or near vacation destinations. Most are situated 10 to 15 miles from urban or suburban shopping areas so that manufacturers don't alienate their department store accounts by selling the same goods virtually next door at a discount.

Manufacturers reaping the benefits of outlet mall popularity include Gap, J. Crew, and Calvin Klein clothiers; West Point Pepperel textiles; Pottery Barn and Crate & Barrel home products; Oneida silversmiths; and Dansk kitchenwares. Top-drawer department stores have also opened outlet stores to sell hard-to-move merchandise. Dillard's has opened a series of clearance centers to make final attempts to move merchandise that failed to sell in the department store. To move their clearance items, Nordstrom operates Nordstrom Rack, Saks Fifth Avenue has Off Fifth, and Neiman Marcus has Last Call.

RESTAURANTS

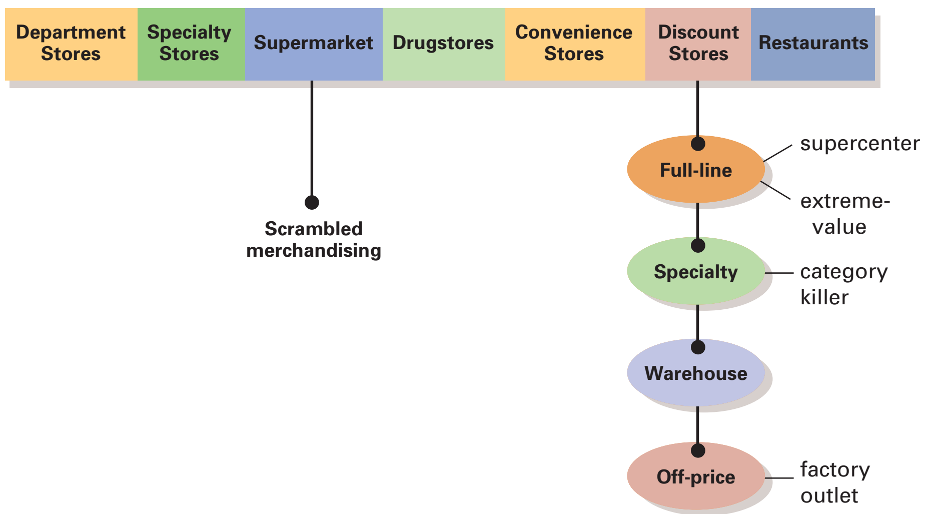
Restaurants straddle the line between retailing establishments and service establishments. Restaurants do sell tangible products—food and drink—but they also provide a valuable service for consumers in the form of food preparation and food service. As a retailing institution, restaurants must deal with many of the same issues as a more traditional retailer, such as personnel, distribution, inventory management, promotion, pricing, and location.

Eating out is an important part of Americans' daily activities and is growing in strength. According to the National Restaurant Association, more than 70 billion meals are eaten in restaurants or cafeterias annually. This means that Americans consume an average of 5.8 commercially prepared meals per week. Food away from home accounts for about 48 percent, or $1,078 per person, of the annual household food budget. The trend toward eating out has been fueled by the increase in working mothers and dual-income families who have more money to eat out and less time to prepare meals at home. The restaurant industry provides work for more than 9 percent of the American workforce and is expected to add 2 million jobs in the next few years, for total employment of 14.8 million people in 2017.[14]

The restaurant industry is one of the most entrepreneurial of businesses and one of the most competitive. Because barriers to entering the restaurant industry are low, the opportunity appeals to many people. The risks, however, are great. About 50 percent of all new restaurants fail within the first year of operation. Restaurants face competition not only from other restaurants but also from the consumer who can easily choose to cook at home. Competition has fostered innovation and ever-changing menus in most segments of the restaurant industry. Many restaurants are now competing directly with supermarkets by offering takeout and delivery in an effort to capture more of the home meal replacement market.

REVIEW LEARNING OUTCOME

LO3 Describe the Major Types of Retail Operations



LO4
Nonstore Retailing

The retailing methods discussed so far have been in-store methods, in which customers must physically shop at stores. In contrast, nonstore retailing is shopping without visiting a store. Because consumers demand convenience, nonstore retailing is currently growing faster than in-store retailing. The major forms of nonstore retailing are automatic vending, direct retailing, direct marketing, and electronic retailing.

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AUTOMATIC VENDING

A low-profile yet important form of retailing is automatic vending, the use of machines to offer goods for sale—for example, the soft drink, candy, or snack vending machines found in college cafeterias and office buildings. Vending is the most pervasive retail business in the United States, with about six million vending machines selling $40 billion annually. Food and beverages account for about 85 percent of all sales from vending machines. Due to the convenience, consumers are willing to pay higher prices for products from a vending machine than for the same products in traditional retail settings.

Retailers are constantly seeking new opportunities to sell via vending. For example, United Artists Theaters offer moviegoers the option of purchasing hot popcorn, Tombstone pizza, Kraft macaroni-and-cheese, and chicken fingers from a vending machine instead of waiting in line at the concession stand. Many vending machines today also sell nontraditional kinds of merchandise, such as videos, toys, stickers, sports cards, office-type supplies, film, and disposable cameras. In a sign of the times, Macy's shoppers can purchase iPod music players and accessories from specially designed Zoom Store vending machines located in select stores.

Of course, vending machines are also an important tool in the ongoing cola wars between Coca-Cola and Pepsi. Both companies are constantly looking for new ways to improve vending machine sales. For example, Coca-Cola is implementing Intelligent Vending, a "cashless" payment system. Vending machines with this system accept credit cards, RFID devices, and hotel room keys and can be accessed via cell phone (mobile e-commerce, or m-commerce, as discussed later in this chapter).[15]

DIRECT RETAILING

In direct retailing, representatives sell products door-to-door, office-to-office, or at home sales parties. Companies like Avon, Mary Kay Cosmetics, The Pampered Chef, Usbourne Books, and World Book Encyclopedia have used this approach for years. But recently direct retailers' sales have suffered as women have entered the workforce. Working women are not home during the day and have little time to attend selling parties. Although most direct sellers like Avon and Silpada still advocate the party plan method, the realities of the marketplace have forced them to be more creative in reaching their target customer. Direct sales representatives now hold parties in offices, parks, and even parking lots. Others hold informal gatherings where shoppers can drop in at their convenience or offer self-improvement classes. Many direct retailers are also turning to direct mail, telephone, or more traditional retailing venues to find new avenues to their customers and increase sales.

nonstore retailing
Selling to consumers through other means than by visiting a store.

automatic vending
The use of machines to offer goods for sale.

direct retailing
The selling of products by representatives who work door-to-door, office-to-office, or at home parties.

Avon, for instance, has begun opening cosmetic kiosk counters, called Avon Beauty Centers, in malls and strip centers. Avon has also launched a new brand—Mark, a beauty "experience" for young women. Most Mark representatives are largely college students who typically sell the product as an after-school, part-time job. Prospective representatives and consumers can buy products or register to be a representative in person, online, or over the phone.[16] Direct retailers are also using the Internet as a channel to reach more customers and increase sales. At Avon's site, individual reps have their own home pages that link from Avon's home page so that sales are credited to them.

In response to the decline in U.S. sales, many long-time direct retailers are exploring opportunities in other countries. For example, Mary Kay, Avon, and Amway have started successful operations in China by adapting their business models to China's laws. Mary Kay agents in China do not purchase and resell the products but are paid a sales commission instead. The company also changed its slogan from "God First, Family Second, Career Third," to "Faith First, Family Second, Career Third."[17]

DIRECT MARKETING

direct marketing (direct-response marketing)
Techniques used to get consumers to make a purchase from their home, office, or another nonretail setting.

According to the Direct Marketing Association, companies spent more than $167 billion on direct marketing in the United States in 2006 and generated about $1.93 trillion in sales.[18] Direct marketing, sometimes called direct-response marketing, refers to the techniques used to get consumers to make a purchase from their home, office, or other nonretail setting. These techniques include direct mail, catalogs and mail order, telemarketing, and electronic retailing. Shoppers using these methods are less bound by traditional shopping situations. Time-strapped consumers and those who live in rural or suburban areas are most likely to be direct-response shoppers because they value the convenience and flexibility that direct marketing provides.

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Direct mailers, such as L.L. Bean's successful catalogs, are created and designed for highly segmented markets. Direct mailers target customers most likely to buy their products by analyzing census data, lifestyle and financial information, and past-purchase and credit history.

Direct Mail

Direct mail can be the most efficient or the least efficient retailing method, depending on the quality of the mailing list and the effectiveness of the mailing piece. With direct mail, marketers can precisely target their customers according to demographics, geographics, and even psychographics. Good mailing lists come from an internal database or from list brokers for about $35 to $150 per thousand names.

Direct mailers are becoming more sophisticated in targeting the "right" customers. Using statistical methods to analyze census data, lifestyle and financial information, and past-purchase and credit history, direct mailers can pick out those most likely to buy their products. So, despite increases in postal rates and raw material and logistics costs, U.S. direct mail services reached $60.6 billion in 2006, an increase of 7.5 percent from 2005.[19] We'll explore how direct marketers are using customer relationship management in Chapter 21.

Catalogs and Mail Order

Consumers can now buy just about anything through the mail, from the mundane, like books, music, and polo shirts, to the outlandish, such as the $5 million diamond-and-ruby-studded bra available through the

Victoria's Secret catalog. Although women make up the bulk of catalog shoppers, the percentage of male catalog shoppers has recently soared. As changing demographics have shifted more of the shopping responsibility to men, they are viewing shopping via catalog, mail order, and the Internet as more sensible than a trip to the mall.

Successful catalogs usually are created and designed for highly segmented markets. For example, Schwan Food Company recently launched Impromptu Gourmet, which offers convenient gourmet and fine dining frozen foods. Certain types of retailers are using mail order successfully. For example, computer manufacturers have discovered that mail order is a lucrative way to sell personal computers to home and small-business users, evidenced by Dell's tremendous success. Dell has used its direct business model to become a $59 billion company and the number one PC seller worldwide. With a global market share of almost 20 percent, it sells over $50 million in computers and equipment online every day.[20]

Telemarketing

telemarketing
The use of the telephone to sell directly to consumers.

Telemarketing is the use of the telephone to sell directly to consumers. It consists of outbound sales calls, usually unsolicited, and inbound calls—that is, orders through toll-free 800 numbers or fee-based 900 numbers.

Rising postage rates and decreasing long-distance phone rates have made *outbound* telemarketing an attractive direct-marketing technique. Skyrocketing field sales costs have also led marketing managers to use outbound telemarketing. Searching for ways to keep costs under control, marketing managers have learned how to pinpoint prospects quickly, zero in on serious buyers, and keep in close touch with regular customers. Meanwhile, they are reserving expensive, time-consuming, in-person calls for closing sales. So many consumers complained about outbound telemarketing calls, however, that Congress passed legislation establishing a national "do not call" list of consumers who do not want to receive unsolicited telephone calls. In addition, Congress passed laws requiring e-mail marketers to allow recipients to opt out of mass e-mails (spam). The laws also prohibit marketers from camouflaging their identity through false return addresses and misleading subject lines. A problem with the telemarketing law, however, is that it exempts nonprofits, so some companies have set up nonprofit subsidiaries to continue their calling activities. Some industry experts say the lists help them by eliminating nonbuyers, but others believe this legislation could have a long-term negative effect on telemarketing sales.[21]

Inbound telemarketing programs, which use 800 and 900 numbers, are mainly used to take orders, generate leads, and provide customer service. Inbound 800 telemarketing has successfully supplemented direct-response TV, radio, and print advertising for more than 25 years.

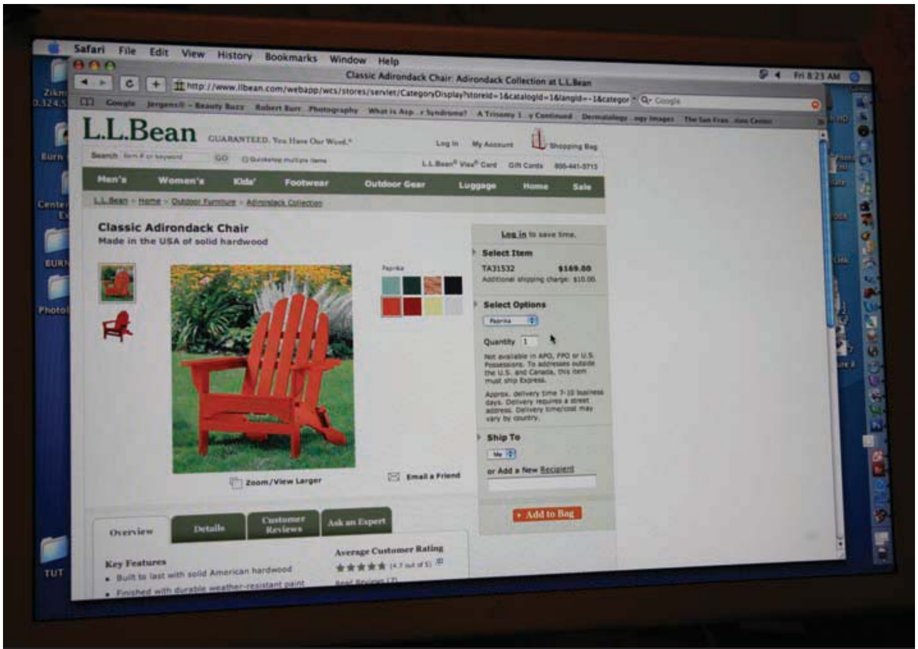
ELECTRONIC RETAILING

Electronic retailing includes the 24-hour, shop-at-home television networks and online retailing.

Shop-at-Home Networks

The shop-at-home television networks are specialized forms of direct-response marketing. Shows display merchandise, with the retail price, to home viewers. Viewers can phone in their orders directly on a toll-free line and shop with a credit card. The shop-at-home industry has quickly grown into a multibillion-dollar business with a loyal customer following. Shop-at-home networks have the capability of reaching nearly every home that has a television set.

The best-known shop-at-home networks are the Home Shopping Network and the QVC (Quality, Value, Convenience) Network. Home shopping networks attract a broad audience through diverse programming and product offerings and are now adding new products to appeal to more affluent audiences. For instance, on QVC, cooking programs attract both men and women, fashion programs attract mostly women, and the NFL Team Shop attracts primarily men. Since it began broadcasting, the channel has sold everything from Sony electronics to Bugs Bunny to Gucci. With annual sales of almost $6 billion, QVC ships more than 150 million packages worldwide to about 10 million customers every year. The company owes its success in part to its customer files of more than 20 million people in 40 countries and to the fact that it introduces as many as 250 new products each week.[22]



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As the popularity of online retailing grows, it is becoming critical that retailers, like L.L. Bean, be online and that their stores, Web sites, and catalogs be integrated. Customers expect to find the same brands, products, and prices whether they purchase online, on the phone, or in a store.

Online Retailing

For years, shopping at home meant looking through catalogs and then placing an order over the telephone. For many people today, however, it now means turning on a computer, surfing retail Web sites, and selecting and ordering products online with the click of a mouse. **Online retailing,** or *e-tailing,* is a type of shopping available to consumers with access to the Internet. Over 70 percent of Americans have Internet access either at home or at work.

online retailing
A type of shopping available to consumers with access to the Internet.

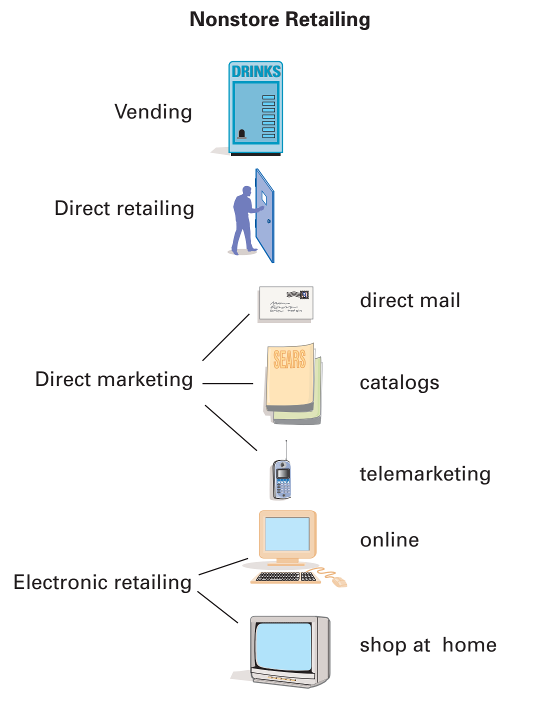
Online retailing has exploded in the last several years as consumers have found this type of shopping convenient and, in many instances, less costly. Consumers can shop without leaving home, choose from a wide selection of merchants, use shopping comparison services to search the Web for the best price, and then have the items delivered to their doorsteps. As a result, online shopping continues to grow at a rapid pace, with online sales accounting for roughly 8 percent of total retail sales. In fact, 2007 online retail sales topped $157 billion and projected to grow to $271.6 billion, or 9 percent of retail sales, by 2011.[23]

Broadcast and cable television networks are cultivating a new source of income by selling products online that are featured in their TV shows. Delivery Agent, a San Francisco company that calls itself the leader in shopping enabled entertainment, manages e-commerce for NBC, Bravo, and Martha Stewart Omnimedia, among others. The producers of Bravo's *Project Runway* contracted with Delivery Agent to sell the clothing designed on the reality fashion competition show. After the challenge to create an outfit for My Scene Barbie, the Bravo.com site sold out of the 3,300 dolls wearing the winning design creation.[24]

As the popularity of online retailing grows, it is becoming critical that retailers be online and that their stores, Web sites, and catalogs be integrated. Customers expect to find the same brands, products, and prices whether they purchase online, on the phone, or in a store. Therefore, retailers are increasingly using in-store kiosks to help tie the channels together for greater customer service. Retailer and cataloger Williams-Sonoma, for example, has linked its store gift registry to its Web site, allowing brides to see who has bought what in real time. Banana Republic stores in New York and Santa Monica, California, have kiosks where customers can order items that aren't on the shelves. Kiosks are even more popular among retailers that target younger, more computer-oriented customers. For example, Van's (**http://www.vans.com**) sells alternative sportswear online as well as in

REVIEW LEARNING OUTCOME

LO4 Discuss nonstore retailing techniques



160 retail stores. Each of its eight skate parks is a combination retail store, entertainment venue, and alternative sports arena. In addition to the skating rink, each park has a lounge area where customers can hang out, watch customized videos, and surf Van's Web site at a bank of kiosks. Each kiosk not only offers a complete selection of Van's footwear, apparel, and accessories, but also includes a full-service pro shop that sells over 500 skateboards, bicycles, helmets, and other equipment and an information center with the latest tour, special event, and contest information.[25]

Online auctions run by Internet companies such as eBay and Amazon.com have enjoyed phenomenal success in recent years. With more than two million items for sale each day, ranging from antique clocks to car stereos, eBay is the leader in cyberspace auctions. Internet auction services like eBay run the Web service and collect a listing fee, plus a commission of 1 to 5 percent when a sale is completed. They also host auctions for other companies. For example, eBay and Sotheby's have a joint venture that offers fine art, rare coins, sports collectibles, jewelry, and antiques online. Each item carries a stamp of authenticity from Sotheby's or one of the 2,800 art and antiques dealers worldwide who have signed exclusive agreements with Sotheby's. The joint venture supports eBay's fine arts and antiques division and enables Sotheby's to offer online sales without the overhead expense of managing its own site.[26]

LO5 Franchising

A *franchise* is a continuing relationship in which a franchisor grants to a franchisee the business rights to operate or to sell a product. The **franchisor** originates the trade name, product, methods of operation, and so on. The **franchisee,** in return, pays the franchisor for the right to use its name, product, or business methods. A franchise agreement between the two parties usually lasts for 10 to 20 years, at which time it can be renewed if both parties are agreeable.

franchisor
The originator of a trade name, product, methods of operation, and so on, that grants operating rights to another party to sell its product.

franchisee
An individual or business that is granted the right to sell another party's product.

To be granted the rights to a franchise, a franchisee usually pays an initial, one-time franchise fee. The amount of this fee depends solely on the individual franchisor, but it generally ranges from $50,000 to $250,000 or higher. In addition to this initial franchise fee, the franchisee is expected to pay royalty fees, usually in the range of 3 to 7 percent of gross revenues. The franchisee may also be expected to pay advertising fees, which usually cover the cost of promotional materials and, if the franchise organization is large enough, regional or national advertising. A McDonald's franchise, for example, costs an initial $45,000 franchise fee. The franchisee must make a down payment of 40 percent of the total cost of a new restaurant or 25 percent of the total cost of an existing restaurant plus a monthly fee based on the restaurant's sales performance and base rent. In addition, a new McDonald's franchisee can expect start-up costs for equipment and pre-opening expenses to range from $506,000 to $1.6 million.[27] The size of the restaurant facility, area of the country, inventory, selection of kitchen equipment, signage, and style of decor and landscaping affect new restaurant costs. Though the dollar amount will vary depending on the type of franchise, fees such as these are typical for all major franchisors, including Burger King, Jani-King, Athlete's Foot, Sonic, and Subway.

Exhibit 15.3

Largest U.S. Franchisors

Rank	Franchisor	Type of Business	Initial Investment
1	7–Eleven Inc	Convenience Store	Varies
2	Subway	Submarine Sandwiches & Salads	$76,100–227,800
3	Dunkin' Donuts	Coffee, Doughnuts, Baked Goods	Varies
4	Pizza Hut	Pizza	$1,100,000–1,700,000
5	McDonald's	Hamburgers, Chicken, Salads	$506,000–1,600,000
6	Sonic Drive In Restaurants	Drive–In Restaurant	$820,000–2,300,000
7	KFC Corp	Chicken	$1,100,000–1,700,000
8	Intercontinental Hotels Group	Hotels	Varies
9	Domino's Pizza LLC	Pizza, Breadsticks, Buffalo Wings	$118,500–460,300
10	Re/Max Int'l, Inc	Real Estate	$35,500–197,000
11	Ups Store, The/Mail Boxes Etc	Postal, Business & Communications Svc	$170,800–279,400
12	Ace Hardware Corp	Hardware & Home Improvement Store	$400,000–1,100,000
13	Jani–King	Commercial Cleaning	$11,300–34,100+
14	Jiffy Lube Int'l, Inc	Fast Oil Change	$214,000–273,000
15	Arby's	Sandwiches, Chicken, Salads	$336,500–2,400,000
16	Baskin–Robbins USA Co	Ice Cream, Frozen Yogurt & Beverages	$156,900–560,400
17	Circle K	Convenience Store	$161,000–1,300,000
18	Kumon Math & Reading Centers	Supplemental Education	$30,400–110,300
19	Great Clips Inc	Hair Salon	$106,900–197,700
20	Bonus Building Care	Commercial Cleaning	$7,600–13,800
21	Jackson Hewitt Tax Service	Tax Preparation Services	$48,600–91,800
22	Taco Bell Corp	Quick–Service Mexican Restaurant	$1,100,000–1,700,000
23	Liberty Tax Service	Income–Tax Preparation Services	$33,800–63,900
24	Super 8 Motels	Economy Motels	$278,900–2,900,000
25	Dairy Queen	Soft–Serve Dairy Products & Sandwiches	$655,000–1,300,000
26	Jan–Pro Franchising Int'l	Commercial Cleaning	$3,300–49,900
27	Blimpie	Submarine Sandwiches & Salads	$142,400–391,200
28	Servpro	Insurance/Disaster Restoration & Cleaning	$100,300–159,200
29	Chem–Dry	Carpet, Drapery & Upholstery Cleaning	$25,300–213,600
30	Matco Tools	Tools	$79,000–182,000

SOURCE: "2008 Franchise 500 Rankings," **http://www.entrepreneur.com,** accessed June 19, 2008.

Exhibit 15.4

Sources of Franchise Information

Some Web sites where people with francising-related questions can find answers:

- **Federal Trade Commission (http://www.ftc.gov)** Has a host of information consumers looking to buy a franchise might need. Click on the "for consumers" link and then on "Franchise & Business Opportunities." Contains information on FTC regulation as well as contact information for state regulators.
- **North American Securities Administrators Association (http://www.nasaa.org)** The umbrella group for state securities regulators offers links to find regulators and also has links to other governmental agencies.
- **International Franchise Association (http://www.franchise.org)** Contains information on such topics as buying a franchise and government relations. The site's FAQ section deals with some issues of franchise regulation.
- **American Franchisee Association (http://www.franchisee.org)** Represents franchisees and has information on legal resources, FTC regulations, and state law.
- **American Association of Franchisees & Dealers (http://www.aafd.org)** Offers legal and financial information.

Franchising is not new. General Motors has used this approach since 1898, and Rexall drugstores, since 1901. Today, there are over half a million franchised establishments in the United States, with combined sales approaching $1.5 trillion, or about 40 percent of all retail trade. Although franchised restaurants attract most of those dollars, hundreds of retail and service franchises, such as Alphagraphics Printshops, Supercuts, and Sylvan Learning Systems, also are thriving. Indeed, there are over 320,000 franchises in 75 industries.[28] Industries expected to see real growth in franchising include home repair, business support services, automotive repairs, hair salons, children's services, and telecommunications. Exhibit 15.3 lists some facts about some of the largest and best-known U.S. franchisors. Exhibit 15.4 lists some Web sites that provide information about franchises.

Two basic forms of franchises are used today: product and trade name franchising and business format franchising. In *product and trade name franchising,* a dealer agrees to sell certain products provided by a manufacturer or a wholesaler. This approach has been used most widely in the auto and truck, soft drink bottling, tire, and gasoline service industries. For example, a local tire retailer may hold a franchise to sell Michelin tires. Likewise, the Coca-Cola bottler in a particular area is a product and trade name franchisee licensed to bottle and sell Coca-Cola's soft drinks.

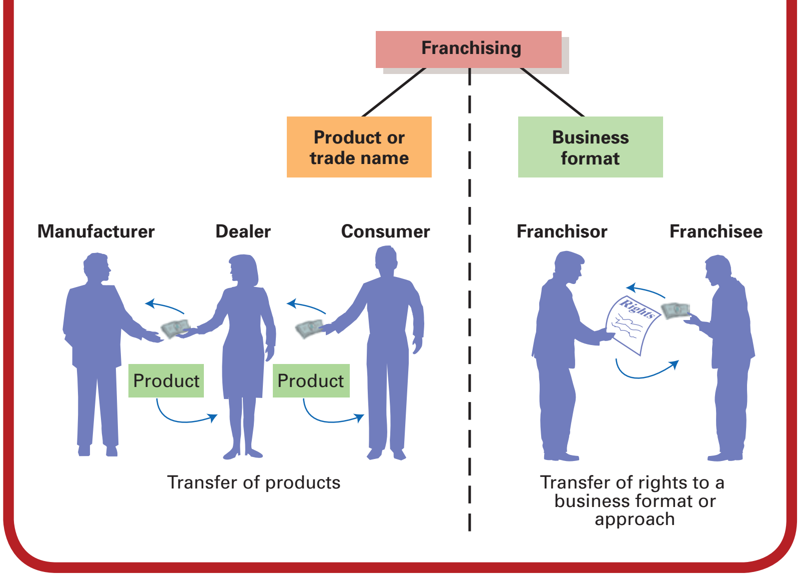
Business format franchising is an ongoing business relationship between a franchisor and a franchisee. Typically, a franchisor "sells" a franchisee the rights to use the franchisor's format or approach to doing business. This form of franchising has rapidly expanded since the 1950s through retailing, restaurant, food-service, hotel and motel, printing, and real estate franchises. Fast-food restaurants like McDonald's, Wendy's, and Burger King use this kind of franchising, as do other companies such as Hyatt Corporation, Unocal Corporation, and ExxonMobil Corporation. To be eligible to be a Domino's Pizza franchisee, you must have worked in a Domino's pizza store for at least one year. The company believes that after working in an existing location, you will have a better understanding of the company and its values and standards. Then potential franchisees must participate in a series of career development, franchise orientation, presentation skills, and franchise development programs.[29]

Like other retailers, franchisors are seeking new growth abroad. Hundreds of U.S. franchisors have begun international expansion and are actively looking for foreign franchisees to open new locations. KFC serves nearly 8 million customers daily at its more than 11,000 restaurants in over 80 countries and territories around the world, including Australia, China, Indonesia, Japan, and Saudi Arabia. KFC's parent company, Yum! Brands, Inc., the world's largest restaurant system, attributes the franchise's success to its ability to adapt to local cultures and tastes without losing control of quality and brand image.[30] The International Franchise Association includes over 100 franchise organizations in countries from Argentina to Zimbabwe.

Franchisors usually allow franchisees to alter their business format slightly in foreign markets. For example, some McDonald's franchisees in Germany sell beer, and in Japan they offer food items that appeal to Japanese tastes, such as steamed dumplings, curry with rice, and roast pork cutlet burgers with melted cheese. McDonald's franchisees in India serve mutton instead of beef because most Indians are Hindu, a religion whose followers believe cows are a sacred symbol of the source of life. The menu also features rice-based Vegetable Burgers made with peas, carrots, red pepper, beans, and Indian spices as well as Vegetable McNuggets. But, in spite of menu differences, McDonald's foreign franchisees still maintain the company's standards of service and cleanliness.

REVIEW LEARNING OUTCOME

LO 5 Define franchising and describe its two basic forms



LO 6
Retail Marketing Strategy

Retailers must develop marketing strategies based on overall goals and strategic plans. Retailing goals might include more traffic, higher sales of a specific item, a more upscale image, or heightened public awareness of the retail operation. The strategies that retailers use to obtain their goals might include a sale, an updated decor, or a new advertisement. The key tasks in strategic retailing are defining and selecting a target market and developing the retailing mix to successfully meet the needs of the chosen target market.

retailing mix
A combination of the six Ps—product, place, promotion, price, presentation, and personnel—to sell goods and services to the ultimate consumer.

product offering
The mix of products offered to the consumer by the retailer; also called the product assortment or merchandise mix.

DEFINING A TARGET MARKET

The first and foremost task in developing a retail strategy is to define the target market. This process begins with market segmentation, the topic of Chapter 8.

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When Beth McLaughlin launched a line of clothing stores, Torrid, aimed exclusively at teenaged girls sizes 12 to 26, she clearly identified her target. Her product offering was tailored to meet that target, as were her choices of location, pricing, and promotion. Torrid has expanded from 6 to 33 stores, with plans for another 19, as a result of McLaughlin's successful strategy.

Successful retailing has always been based on knowing the customer. Sometimes retailing chains flounder when management loses sight of the customers the stores should be serving.

Target markets in retailing are often defined by demographics, geographics, and psychographics. For instance, Bluefly.com, a discount fashion e-tailer, targets both men and women in their thirties, who have a higher-than-average income, read fashion magazines, and favor high-end designers. By understanding who its customers are, the company has been able to tailor its Web site to appeal specifically to its audience. The result is a higher sales rate than most clothing e-tailers, rating number 131 in the Internet Retailer Top 500 Guide.[31]

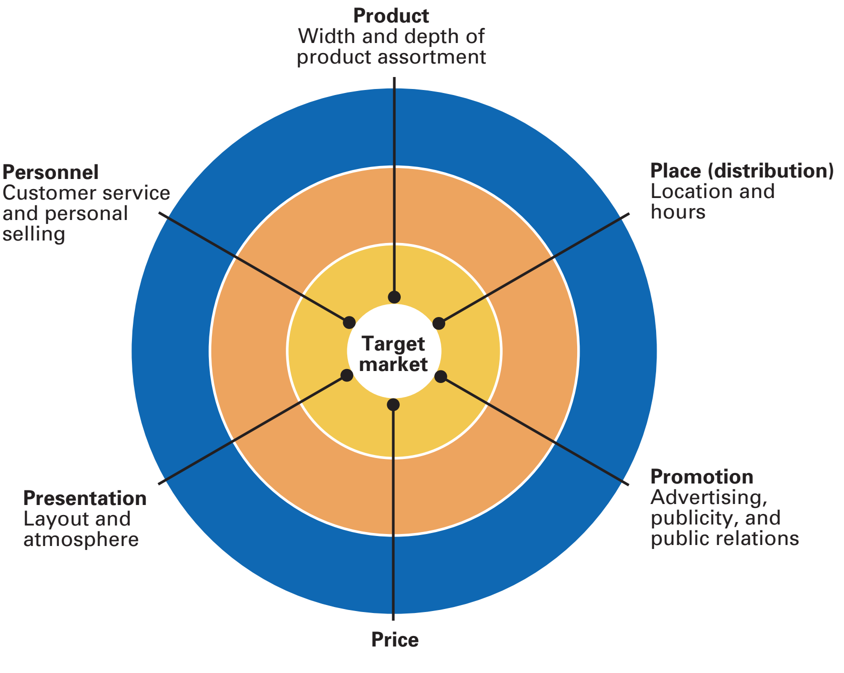
Determining a target market is a prerequisite to creating the retailing mix. For example, Target's merchandising approach for sporting goods is to match its product assortment to the demographics of the local store and region. The amount of space devoted to sporting goods, as well as in-store promotions, also varies according to each store's target market.

CHOOSING THE RETAILING MIX

Retailers combine the elements of the retailing mix to come up with a single retailing method to attract the target market. The **retailing mix** consists of six Ps: the four Ps of the marketing mix (product, place, promotion, and price) plus presentation and personnel (see Exhibit 15.5).

The combination of the six Ps projects a store's image, which influences consumers' perceptions. Using these impressions of stores, shoppers position one store against another. A retail marketing manager must make sure that the store's positioning is compatible with the target customers' expectations. As discussed at the beginning of the chapter, retail stores can be positioned on three broad dimensions: service provided by store personnel, product assortment, and price. Management should use everything else—place, presentation, and promotion—to fine-tune the basic positioning of the store.

Exhibit 15.5
The Retailing Mix



The Product Offering

The first element in the retailing mix is the **product offering,** also called the *product assortment* or *merchandise mix*. Retailers decide what to sell on the basis of what their target market wants to buy. They can base their decision on market research, past sales, fashion trends, customer requests, and other sources. A recent approach, called data mining, uses complex mathematical models to help retailers make better product mix decisions. Early users of the approach, such as Dillard's, Target, and Wal-Mart, use data mining to

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determine which products to stock at what price, how to manage markdowns, and how to advertise to draw target customers.

Developing a product offering is essentially a question of the width and depth of the product assortment. *Width* refers to the assortment of products offered; *depth* refers to the number of different brands offered within each assortment. Price, store design, displays, and service are important to consumers in determining where to shop, but the most critical factor is merchandise selection. This reasoning also holds true for online retailers. Amazon.com, for instance, is building the world's biggest online department store so that shoppers can get whatever they want with one click on their Web browsers. Like a traditional department store or mass merchandiser, Amazon offers considerable width in its product assortment with millions of different items, including books, music, toys, videos, tools and hardware, health and beauty aids, electronics, and software. Conversely, online specialty retailers, such as 1-800-Flowers.com, gloss.com (makeup), and polo.com (clothing), focus on a single category of merchandise, hoping to attract loyal customers with a larger depth of products at lower prices and better customer service. Many online retailers purposely focus on single product line niches that could never garner enough foot traffic to support a traditional brick-and-mortar store.

After determining what products will satisfy target customers' desires, retailers must find sources of supply and evaluate the products. When the right products are found, the retail buyer negotiates a purchase contract. The buying function can either be performed in-house or be delegated to an outside firm. The goods must then be moved from the seller to the retailer, which means shipping, storing, and stocking the inventory. The trick is to manage the inventory by cutting prices to move slow goods and by keeping adequate supplies of hot-selling items in stock. As in all good systems, the final step is to evaluate the entire process to seek more efficient methods and eliminate problems and bottlenecks.

As margins drop and competition intensifies, retailers are becoming ever more aware of the advantages of *private brands,* or those brands that are designed and developed using the retailer's name. Because the cost of goods typically makes up between 60 and 75 percent of a retailer's expenses, eliminating intermediaries can shave costs. As a result, prices of private-label goods are typically lower than for national brands, giving customers greater value. Private-label branding is not new. For decades, Sears has fashioned its Kenmore, Craftsman, and DieHard brands into household names. Wal-Mart has several successful private-label brands such as White Cloud paper products, Spring Valley nutritional supplements, Sam's American Choice laundry detergent, EverActive alkaline batteries, and EverStart auto batteries. Its Ol' Roy dog food and Sam's American Choice garden fertilizer are now the best-selling brands in their categories.

Promotion Strategy

Retail promotion strategy includes advertising, public relations and publicity, and sales promotion. The goal is to help position the store in consumers' minds. Retailers design intriguing ads, stage special events, and develop promotions aimed at their target markets. Today's grand openings are a carefully orchestrated blend of advertising, merchandising, goodwill, and glitter. All the elements of an opening—press coverage, special events, media advertising, and store displays—are carefully planned. For example, when Victoria's Secret opened its megastore in Dallas, the opening featured a $150 gift with a $50 purchase, free makeovers from a Victoria's Secret Fashion Show makeup artist, $10 gift cards that could be redeemed in the store, and an appearance by supermodel Heidi Klum.

Retailers' advertising is carried out mostly at the local level. Local advertising by retailers usually provides specific information about their stores, such as location, merchandise, hours, prices, and special sales. In contrast, national retail advertising generally focuses on image. For example, Target has used its "sign of the times" advertising campaign to effectively position itself as the "chic place to buy cheap."

Target's advertising campaign also takes advantage of cooperative advertising, another popular retail advertising practice. Traditionally, marketers would pay retailers to feature their products in store mailers, or a marketer would develop a TV campaign for the product and simply tack on several retailers' names at the end. But Target's advertising makes use of a more collaborative trend by integrating products such as Tide laundry detergent, Tums antacids, or Coca-Cola into the actual campaign. Another common form of cooperative advertising involves promotion of exclusive products. For example, Target hires famous designers to develop reasonably priced product lines available exclusively at Target stores.

Many retailers are forgoing media advertising these days in favor of direct-mail or frequent shopper programs. Direct-mail and catalog programs are luring many retailers, which hope they will prove to be a cost-effective means of increasing brand loyalty and spending by core customers. Nordstrom, for example, mails catalogs featuring brand-name and private-brand clothing, shoes, and accessories to target the shop-at-home crowd. Restaurants and small retailers have successfully used frequent diner or frequent shopper programs for years. For example, customers with a Victoria's Secret Angel credit card are offered monthly specials on store merchandise, including items that generally are not put on sale to the public.

The Proper Location

The retailing axiom "location, location, location" has long emphasized the importance of place to the retail mix. The location decision is important first because

GLOBAL Perspectives

Luxury Retail Goes Global

These days, developing countries are consistently winning out when it comes to luxury retail investments. The most attractive of these emerging markets include China, India, Russia, Brazil, the United Arab Emirates, South Africa, Vietnam, Malaysia, and Indonesia. Juicy Couture's founders say they have 63 stores in the U.S., and within ten years, they'll have 47 in Asia. Malaysia, a country that does not even aim to achieve "developed" status until 2020, suddenly boasts one of the most prestigious luxury shopping malls in Asia. In Dubai, designer boutiques such as Harvey Nichols, Marc Jacobs, and Missoni entice luxury shoppers to the Mall of the Emirates—winner of the "Retail Destination of the Year" award.

In China, a booming economy has driven the emergence of new millionaires and a new middle class with money to spend. And spend they do—especially on luxury shoes, handbags, cars, and jewelry. Cartier recently created a massive ice replica of its flagship Paris jewelry store at a winter festival in Harbin city as part of its bid to become a well-known prestige brand there. After nearly doubling its sales in China in recent years, Cartier plans to build another 30 boutique stores across China—more stores than it has in any other country other than the United States. Such confidence is merited—industry analysts expect the Chinese to purchase at least 30 percent of the world's luxury goods in the next ten years.

India's retail market is expected to nearly double to $635 billion by 2015. Retail analysts have gone so far as to call India's current economic climate a "retail gold rush." This could be in part because of India's recently relaxed retail laws that finally allow foreign, single-brand retailers to own a majority interest, or 51 percent, of a joint venture with a local partner. That was just the incentive luxury retail conglomerates were waiting for it seems, as many rushed to build freestanding stores in India's largest cities. For example, Gucci built a 3,400 square-foot boutique—the largest luxury retail unit in India—in partnership with the Indian apparel conglomerate Murjani Group in Mumbai. Access to attractive building sites is a continuing challenge to retailers hoping to move into India's wealthy cities; many are limited to hotel shopping arcades. Murjani Group, however, hired European architects to design its freestanding retail stores. Mohan Murjani himself said, "At the end of the day, the Indian consumer doesn't want to feel like they are going to Gucci in India. They should feel like they have walked into Gucci, period. It has to be world class." The Murjani Group plans to establish 500 new, freestanding, single-brand retail stores in India over the next five years.

Luxury and fashion companies are similarly flocking to Russia to take advantage of that country's growing petroleum-fueled wealth. Department stores in Russia that 20 years ago were stocked with pots, pans, and homey scarves, are now home to a variety of designer shops such as Dior, Cartier, Gucci, Louis Vuitton, and Hermés. Moscow's mayor just recently built a $350 million, three-story, underground mall loaded with 100 designer stores such as Tommy Hilfiger, Yves Rocher, and Diesel.

Why do you think luxury goods brands are opening stores in emerging markets? How do you think technology has contributed to the expanding global luxury market? The World Bank estimates that more than 600 million people in Asia live on less than a dollar a day. How do you suppose luxury goods purveyors thrive there? [32]

the retailer is making a large, semipermanent commitment of resources that can reduce its future flexibility. Second, the location will affect the store's future growth and profitability.

Site location begins by choosing a community. Important factors to consider are the area's economic growth potential, the amount of competition, and geography. For instance, retailers like T. J. Maxx, Wal-Mart, and Target build stores in areas where the population is growing. Often these large retailers will build stores in new communities that are still under development. On the other hand, while population growth is an important consideration for fast-food restaurants, most also look for an area with other fast-food restaurants because being located in clusters helps to draw customers for each restaurant. However, even after careful research the perfect position can be elusive in the face of changing markets. For example, Wendy's found when attempting to enter the competitive breakfast business that its locations weren't positioned on the right side of the road to attract the bulk of commuters looking for breakfast.[33] Finally, for many retailers geography remains the most important factor in choosing a community. For example, Starbucks coffee looks for densely populated urban communities for its stores, Talbots looks for locations near upper-class neighborhoods, and Buckle stores look for locations in small, underserved cities.

destination stores
Stores that consumers purposely plan to visit.

After settling on a geographic region or community, retailers must choose a specific site. In addition to growth potential, the important factors are neighborhood socioeconomic characteristics, traffic flows, land costs, zoning regulations, and public transportation. A particular site's visibility, parking, entrance and exit locations, accessibility, and safety and security are also considered. Additionally, a retailer should consider how its store would fit into the surrounding environment. Retail decision makers probably would not locate a Dollar General store next door to a Neiman Marcus department store.

Retailers face one final decision about location: whether to have a freestanding unit or to become a tenant in a shopping center or mall.

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For supercenter retailers such as Target, offering almost everything a customer might want under one roof—including designer clothing, groceries, and pharmacy items—makes their customer more likely to make their store a one-stop destination.

Freestanding Stores

An isolated, freestanding location can be used by large retailers like Wal-Mart or Target and sellers of shopping goods like furniture and cars because they are "destination" stores. Destination stores are stores consumers seek out and purposely plan to visit. An isolated store location may have the advantages of low site cost or rent and no nearby competitors. On the other hand, it may be hard to attract customers to a freestanding location, and no other retailers are around to share costs.

Freestanding units are increasing in popularity as retailers strive to make their stores more convenient to access, more enticing to shop, and more profitable. Freestanding sites now account for more than half of all retail construction in the United States as more and more retailers are deciding not to locate in pedestrian malls. Perhaps the greatest reason for developing a freestanding site is greater visibility. Retailers often feel they get lost in huge centers and malls, but freestanding units can help stores develop an identity with shoppers. The ability to grow at faster rates through freestanding buildings has also propelled the surge toward stand-alone units. Retailers like The Sports Authority, Linens N Things, Best Buy, and Bed Bath & Beyond choose to be freestanding to achieve their expansion objectives. An aggressive expansion plan may not allow time to wait for shopping centers to be built. Similarly, drugstore chains like Walgreens and Rite-Aid have been aggressively relocating their existing mall and shopping center stores to freestanding sites, especially street corner sites for drive-through accessibility.

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In addition to being commercial centers, shopping malls were once a hub of community social activity. Lately, however, malls have struggled to compete against newer lifestyle centers and freestanding stores. Even with 520 stores, Mall of America regularly adds rides to its entertainment section to attract shoppers.

Shopping Centers Shopping centers began in the 1950s when the U.S. population started migrating to the suburbs. The first shopping centers were *strip centers,* typically located along busy streets. They usually included a supermarket, a variety store, and perhaps a few specialty stores. Then *community shopping centers* emerged, with one or two small department stores, more specialty stores, a couple of restaurants, and several apparel stores. These community shopping centers provided off-street parking and a broader variety of merchandise.

Regional malls offering a much wider variety of merchandise started appearing in the mid-1970s. Regional malls are either entirely enclosed or roofed to allow shopping in any weather. Most are landscaped with trees, fountains, sculptures, and the like to enhance the shopping environment. They have acres of free parking. The *anchor stores* or *generator stores* (JCPenney, Sears, or major department stores) are usually located at opposite ends of the mall to create heavy foot traffic. Las Vegas's Fashion Show Mall takes the concept to the extreme. The mall has 2 million square feet of retail space and boasts over 250 stores, eight of which are anchor stores, including Neiman Marcus, Saks Fifth Avenue, Macy's, Bloomingdale Home, and Nordstrom. Mall of America goes even further, with 2.5 million square feet of retail space and over 520 stores.

According to shopping center developers, the newest generation of shopping centers are *lifestyle centers*. These new open-air shopping centers are targeted to upper-income shoppers with an aversion for "the mall" and seek to create an atmosphere that is part neighborhood park and part urban shopping center. Lifestyle centers typically combine outdoor shopping areas comprised of upscale retailers and restaurants, with plazas, fountains, and pedestrian streets. Newer centers like the Easton Town Center in Columbus, Ohio and the Legacy Town Center in Plano, Texas, also include luxury apartments and condominiums. Lifestyle centers are appealing to retail developers looking for an alternative to the traditional shopping mall, a concept rapidly losing favor among shoppers. Consumers have also become more pressed for time in recent years and are choosing more convenient stand-alone stores and neighborhood centers instead of malls. Faced with this trend, mall developers have improved the layout of many malls to make it more convenient for customers to shop. For instance, the RiverTown Crossings center in Grandville, Michigan, clusters competing stores, like Abercrombie Kids, GapKids, Gymboree, and other kids' clothing stores in one section of the mall to accommodate time-strapped parents.[34] Locating in a community shopping center or regional mall offers several advantages and disadvantages, as shown in Exhibit 15.6.

Exhibit 15.6

Advantages and Disadvantages of Locating in a Community Shopping Center or Regional Mall

Advantages	Disadvantages
facilities present a unified image and are designed to attract shoppers	expensive leases
tenants share the expenses of the mall's common area and promotions for the whole mall	common promotion efforts might not attract customers to a particular store
the shopping environment, anchor stores, and "village square" activities draw customers	anchor stores dominate the tenants' association
malls can target different demographic groups, such as upscale or bargain shoppers	possibility of having direct competitors within the same facility
ample parking is available	lease restrictions on merchandise carried and hours of operation

Retail Prices

Another important element in the retailing mix is price. Retailing's ultimate goal is to sell products to consumers, and the right price is critical in ensuring sales. Because retail prices are usually based on the cost of the merchandise, an essential part of pricing is efficient and timely buying.

Price is also a key element in a retail store's positioning strategy. Higher prices often indicate a level of quality and help reinforce the prestigious image of retailers, such as Tiffany, Saks Fifth Avenue, Gucci, Cartier, and Neiman Marcus. On the other hand, discounters and off-price retailers, such as Target and T. J. Maxx, offer good value for the money. There are even stores, such as Dollar Tree, where everything costs one dollar. Dollar Tree's single-price-point strategy is aimed at getting customers to make impulse purchases through what analysts call the "wow factor"—the excitement of discovering that an item costs only a dollar.

A pricing trend among American retailers that seems to be here to stay is *everyday low pricing,* or EDLP. Introduced to the retail industry by Wal-Mart, EDLP offers consumers a low price all the time rather than holding periodic sales on merchandise. Even large retail giants, like Macy's, Inc., have phased out deep discounts and sales in favor of lower prices every day. Similarly, Gap reduced prices on denim jeans, denim shirts, socks, and other items to protect and broaden the company's share of the casual clothes market. Supermarkets such as Albertson's and Winn-Dixie have also found success in EDLP.

atmosphere
The overall impression conveyed by a store's physical layout, decor, and surroundings.

Presentation of the Retail Store

The presentation of a retail store helps determine the store's image and positions the retail store in consumers' minds. For instance, a retailer that wants to position itself as an upscale store would use a lavish or sophisticated presentation.

The main element of a store's presentation is its **atmosphere,** the overall impression conveyed by a store's physical layout, decor, and surroundings. The atmosphere might create a relaxed or busy feeling, a sense of luxury or of efficiency, a friendly or cold attitude, a sense of organization or of clutter, or a fun or serious mood. For example, Wolfgang Puck restaurants feature tiles in the shape of a pizza on the floors, walls, and countertops. Urban Outfitters stores, targeted to Generation Y consumers, use raw concrete, original brick, rusted steel, and unfinished wood to convey an urban feel. Likewise, REI sporting-goods stores feature indoor rock-climbing walls, bike test trails, and rain rooms for testing outdoor gear.

The layout of retail stores is a key factor in their success. The goal is to use all space in the store effectively, including aisles, fixtures, merchandise displays, and nonselling areas. In addition to making shopping easy and convenient for the customer, an effective layout has a powerful influence on customer traffic patterns and purchasing behavior. For instance, Kohl's unique circular layout encourages customers to pass all of a store's departments to reach the checkout lanes. The stores are smaller than most department stores but have a wide aisle with plenty of room for customers and shopping carts. Each department is limited to five display racks on the main

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When not actually browsing or buying, people enjoy a comfortable and memorable experience in a shopping environment. Shopping malls and lifestyle centers now provide shoppers with kids' play towns and parents' rooms for retreating with babies and toddlers.

aisle. Displays are spaced widely and are set at varying heights so that customers can see everything in the department, including wall displays, from the main aisle. To further enhance the store's clean crisp presentation, merchandise is displayed from light to dark, which research suggests is most pleasing to the eye. Finally, to encourage last-minute, impulse purchases, Kohl's displays low-cost items at the checkout register. Together with other merchandising strategies, the store layout generates an average of over $300 in sales per square foot (this is a standard industry measure) in Kohl's almost 750 stores in 41 states and contributed to a sales increase of almost 15 percent in 2005.[35]

Layout also includes where products are placed in the store. Many technologically advanced retailers are using a technique called *market-basket analysis* to analyze the huge amounts of data collected through their point-of-purchase scanning equipment. The analysis looks for products that are commonly purchased together to help retailers place products in the right places. Wal-Mart uses market-basket analysis to determine where in the store to stock products for customer convenience.[36] In a typical Wal-Mart Supercenter, bananas are placed not only in the produce section but also in the cereal aisle. Kleenex tissues are in the paper-goods aisle and also mixed in with the cold medicines. Measuring spoons are in the housewares and also hanging next to Crisco shortening. During October, flashlights are with the Halloween costumes as well as in the hardware aisle.

These are the most influential factors in creating a store's atmosphere:

- *Employee type and density:* Employee type refers to an employee's general characteristics—for instance, neat, friendly, knowledgeable, or service oriented. Density is the number of employees per thousand square feet of selling space. A discounter like Kmart has a low employee density that creates a "do-it-yourself," casual atmosphere. In contrast, Neiman Marcus's density is much higher, denoting readiness to serve the customer's every whim. Too many employees and not enough customers, however, can convey an air of desperation and intimidate customers.
- *Merchandise type and density:* The type of merchandise carried and how it is displayed add to the atmosphere the retailer is trying to create. A prestigious retailer like Saks or Bloomingdale's carries the best brand names and displays them in a neat, uncluttered arrangement. Discounters and off-price retailers, such as Marshall's and T. J. Maxx, may sell some well-known brands, but many carry seconds or out-of-season goods. Their merchandise is crowded into small spaces and hung on long racks by category—tops, pants, skirts, etc.—to create the impression that "We've got so much stuff, we're practically giving it away."
- *Fixture type and density:* Fixtures can be elegant (rich woods), trendy (chrome and smoked glass), or consist of old, beat-up tables, as in an antiques store. The fixtures should be consistent with the general atmosphere the store is trying to create. Apple has let its focus on design inform the look of its retail stores. Many Apple stores contain a signature glass staircase designed in part by CEO Steve Jobs, and all use large open tables to display company products. Because products are not cluttered on store shelves, it is easier for store visitors to play with them.[37]
- *Sound:* Sound can be pleasant or unpleasant for a customer. Classical music at a nice Italian restaurant helps create ambience, just as country-and-western music does at a truck stop. Music can also entice customers to stay in the store longer and buy more or eat quickly and leave a table for others. For instance, rapid music tends to make people eat more, chew less, and take bigger bites, whereas slow music prompts people to dine more leisurely and eat less. Retailers can tailor their musical atmosphere to their shoppers' demographics and the merchandise they're selling. Music can control the pace of the store traffic, create an image, and attract or direct the shopper's attention. Starbucks has

parlayed its unique in-store music selections into a new business with its Hear Music Channel on XM Satellite Radio, its Hear Music Cafés, and kiosks selling featured Hear Music artists in most Starbucks locations.

- *Odors:* Smell can either stimulate or detract from sales. The wonderful smell of pastries and breads entices bakery customers. Conversely, customers can be repulsed by bad odors such as cigarette smoke, musty smells, antiseptic odors, and overly powerful room deodorizers. If a grocery store pumps in the smell of baked goods, sales in that department increase threefold. Department stores have pumped in fragrances that are pleasing to their target market, and the response has been favorable. Not surprisingly, retailers are increasingly using fragrance as a key design element, as important as layout, lighting, and background music. Research suggests that people evaluate merchandise more positively, spend more time shopping, and are generally in a better mood when an agreeable odor is present. Retailers use fragrances as an extension of their retail strategy.
- *Visual factors:* Colors can create a mood or focus attention and therefore are an important factor in atmosphere. Red, yellow, and orange are considered warm colors and are used when a feeling of warmth and closeness is desired. Cool colors like blue, green, and violet are used to open up closed-in places and create an air of elegance and cleanliness. For example, Starbucks Coffee uses an eggplant, golden yellow, and dark olive color combination so that customers will feel comfortable yet sophisticated. Some colors are better for display. For instance, diamonds appear most striking against black or dark blue velvet. Lighting can also have an important effect on store atmosphere. Jewelry is best displayed under high-intensity spotlights and cosmetics under more natural lighting. Many retailers have found that natural lighting, either from windows or skylights, can lead to increased sales. Outdoor lighting can also affect consumer patronage. Consumers often are afraid to shop after dark in many areas and prefer strong lighting for safety. The outdoor facade of the store also adds to its ambience and helps create favorable first impressions.

Personnel and Customer Service

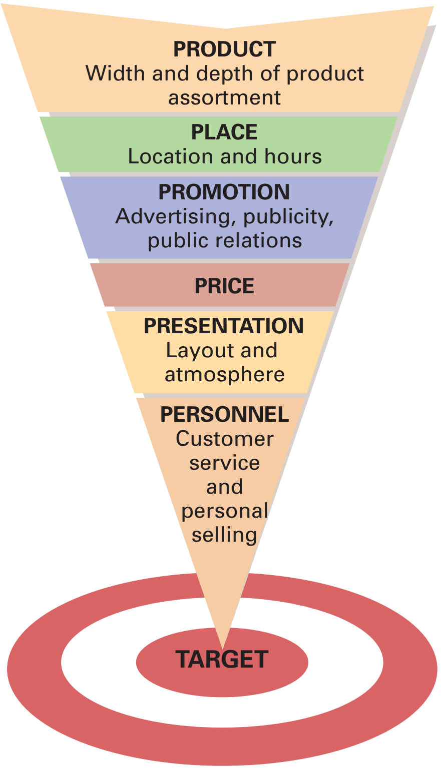
People are a unique aspect of retailing. Most retail sales involve a customer–salesperson relationship, if only briefly. When customers shop at a grocery store, the cashiers check and bag their groceries. When customers shop at a prestigious clothier, the salesclerks may help select the styles, sizes, and colors. They may also assist in the fitting process, offer alteration services, wrap purchases, and even offer a glass of champagne. Sales personnel provide their customers with the amount of service prescribed in the retail strategy of the store.

Retail salespeople serve another important selling function: They persuade shoppers to buy. They must therefore be able to persuade customers that what they are selling is what the customer needs. Salespeople are trained in two common selling techniques: trading up and suggestion selling. Trading up means persuading customers to buy a higher-priced item than they originally intended to buy. To avoid selling customers something they do not need or want, however, salespeople should take care when practicing trading-up techniques. Suggestion selling, a common practice among most retailers, seeks to broaden customers' original purchases with related items. For example, if you buy a new printer at Office Depot, the sales representative will ask if you would like to purchase paper, a USB cable, and/or extra ink cartridges. Similarly, McDonald's cashiers are trained to ask customers if they would like a hot apple pie with their hamburger and fries. Suggestion selling and trading up should always help shoppers recognize true needs rather than sell them unwanted merchandise.

Providing great customer service is one of the most challenging elements in the retail mix because customer expectations change. Ten years ago, shoppers wanted personal one-on-one attention. Today, most customers are happy to help themselves

REVIEW LEARNING OUTCOME

LO6 List the major tasks involved in developing a retail marketing strategy



as long as they can easily find what they need. In addition, customer expectations for service vary considerably. What customers expect in a department store is very different from their expectations for a discount store. Luxury retailers, for whom extreme customer service has always been a hallmark, are beginning to add a new level of service personnel to their high-profile locations: the store concierge. Concierges routinely fulfill customer requests that have nothing to do with shopping. Gary Jackson is the concierge for the Dallas store of luxury retailer Barneys New York. He has called a new private club to get a customer on the guest list and has squired another customer's college-age daughter and her out-of-town guests around to Dallas's newest nightspots. When one customer ripped a pair of pants and needed replacements that matched his suit jacket before an important meeting the next morning, Jackson delivered a selection of pants to the customer's hotel room at 11 P.M. the night before.[38]

Customer service is also critical for online retailers. Online shoppers expect a retailer's Web site to be easy to use, products to be available, and returns to be simple. Therefore, customer-friendly retailers like Bluefly.com design their sites to give their customers the information they need such as what's new and what's on sale. Other companies like Amazon.com and LandsEnd.com offer product recommendations and personal shoppers. Some retailers that have online, catalog, and traditional brick-and-mortar stores, such as Lands' End, Gap, and Williams-Sonoma, now allow customers to return goods bought through the catalog or online to their traditional store to make returns easier.

LO7 New Developments in Retailing

In an effort to better serve their customers and attract new ones, retailers are constantly adopting new strategies. Four recent developments are interactivity, m-commerce, pop-up shops, and the store-in-a-store model.

INTERACTIVITY

Adding interactivity to the retail environment is one of the most popular strategies in retailing in the past few years. Small retailers as well as national chains are using interactivity in stores to differentiate themselves from the competition. For some time, retailers have used "entertainment" retailing in the form of playing music, showing videos, hosting special events, and sponsoring guest appearances, but the new interactive trend gets customers involved rather than just catching their eye. For example, at the American Girl store in Chicago, customers can purchase a doll made to look like them, take their dolls to the in-store American Girl café, go to the American Girl Theater, and even have their birthday parties. Similarly, Build-A-Bear enables customers to make their own stuffed animal by choosing which animal to stuff and then dressing and naming it. You can hold birthday parties there, too.

Involvement isn't just for children, either. For Your Entertainment, one of the country's leading specialty retailers of movies, music, and games, regularly invites artists to perform in its stores. Performers may be local favorites or national superstars. FYE even has a MySpace site that features a state-by-state touring schedule and allows local performers to sign up to play at its stores. Fans can request to see a local group perform at an FYE store or ask the stores to stock recordings by their local favorites.[39]

M-COMMERCE

M-commerce (mobile e-commerce) enables consumers using wireless mobile devices to connect to the Internet and shop. Essentially, m-commerce goes beyond text message advertisements to allow consumers to purchase goods and services using wireless mobile devices, such as mobile telephones, pagers, personal digital assistants (PDAs), and handheld computers. For example, both PepsiCo and Coca-Cola have developed smart vending technologies. Coca-Cola's Intelligent Vending, a "cashless" payment system, accepts credit cards, RFID devices, and hotel room keys, and can be accessed via cell phone.[40] M-commerce enjoyed early success overseas, but has been slower in gaining acceptance and popularity in the United States. In 2006, for instance, there were over 95 million wireless subscribers in Japan but more than 200 million in the United States. However, only about $480 million in revenue was generated by about 7 million U.S. m-commerce users compared to Japan's 27 million m-commerce users generating $10 billion in sales. One research company in the U.K., Juniper Research, predicts that the global m-commerce market will reach $88 billion by 2009.[41]

M-commerce users adopt the new technology because it saves time and offers more convenience in a greater number of locations. Vending machines have become an important venue for m-commerce. In the first quarter of 2007 alone, nearly 74 million Americans subscribed to mobile Internet providers to search, e-mail, and check weather and sports. Even so, the U.S. is an immature market compared to Japan and Western Europe.

pop-up shops
Temporary retail establishments that provide flexible locations without a long-term commitment.

REVIEW LEARNING OUTCOME

LO7 Describe new developments in retailing

Interactivity gets consumers involved in retail experience.

M-commerce is purchasing goods through mobile devices.

Pop-up shops provide flexible locations without long-term commitment.

Small stores within larger stores—a store-in-a-store—provide shopping convenience.

POP-UP SHOPS

Companies of all sizes are experimenting with pop-up shops. As the name implies, pop-up shops are temporary retail establishments that allow companies flexible locations without the long-term commitment of a more expensive retail lease. Italian coffee maker illy opened a pop-up shop at Time Warner Center in New York for ten days. In addition to selling coffee, the illy shop, created from a shipping container, offered free samples from the company's soon-to-be-released Hyper Espresso System machine.[42] Pop-up shops aren't always sized like kiosks, however. Toys 'R' Us opened a 25,000-square-foot temporary store in the former Tower Records building during the Christmas 2007 shopping season.[43]

Wired magazine incorporated interactivity in its 2007 holiday pop-up shop. Customers could try out over 100 of the latest techie toys and participate in a SoHo scavenger hunt (contestants used a Palm Centro to navigate through the game) for a chance at winning a Nintendo Wii.[44]

STORE IN A STORE

Another trend in retailing is the store-in-a-store model. Companies as diverse as Levenger (whose tagline is "Tools for Serious Readers"), Apple, Kolo (an international photo album company), Procter & Gamble, and more have used the store-in-a-store concept. Levenger has small stores inside two Chicago Macy's locations; Apple has stores in various Best Buy stores in the United States and FNAC stores in France; Kolo opened a 450-square-foot Kolo Boutique inside Kate's Paperie, a famous stationery store in Soho; and Procter & Gamble has dedicated shops for health and beauty inside certain Royal Ahold grocery stores.[45]

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percentage of retailers operating just one store > **90**

10 < percentage of the capability of new electronic gear actually used by consumers

prescriptions purchased by the average 60-year old each year > **15**

177 < SuperTarget locations in the U.S.

cost of the diamond solitaire ring offered by Sam's Club at Christmas time > **$347,000**

70 billion < meals Americans eat in restaurants and cafeterias each year

Dell's daily online sales of computers and equipment > **$50 million**

250 < new products introduced on QVC each week

percentage of Americans with Internet access at home or work > **70**

80 < countries with KFC franchises

Review and Applications

LO 1

Discuss the importance of retailing in the U.S. economy. Retailing plays a vital role in the U.S. economy for two main reasons. First, retail businesses contribute to our high standard of living by providing a vast number and diversity of goods and services. Second, retailing employs a large part of the U.S. working population—over 15 million people.

1.1 To fully appreciate the role retailing plays in the U.S. economy, it may be helpful to review a selection of press articles related to the retailing industry. Search for articles pertaining to retailing. Read a selection of articles, and report your findings to the class.

1.2 Keep a shopping journal that details all the retail establishments you visit in a week, how long you spent in each store, how much money you spent, and the reason for your visit. At the end of the week, review your journal and analyze your relationship to retail. As a class, compile your results to get a picture of shopping habits and consumer behavior.

LO 2

Explain the dimensions by which retailers can be classified. Many different kinds of retailers exist. A retail establishment can be classified according to its ownership, level of service, product assortment, and price. On the basis of ownership, retailers can be broadly differentiated as independent retailers, chain stores, or franchise outlets. The level of service retailers provide can be classified along a continuum of high to low. Retailers also classify themselves by the breadth and depth of their product assortments; some retailers have concentrated product assortments, whereas others have extensive product assortments. Last, general price levels also classify a store, from discounters offering low prices to exclusive specialty stores where high prices are the norm. Retailers use these latter three variables to position themselves in the marketplace.

2.1 Form a team of three classmates to identify different retail stores in your city where pet supplies are sold. Include nonstore forms of retailing, such as catalogs, the Internet, or the local veterinarian. Team members should divide up and visit all the different retailing outlets for pet supplies. Prepare a report describing the differences in brands and products sold at each of the retailing formats and the differences in store characteristics and service levels. For example, which brands are sold via mass merchandiser, independent specialty store, or other venue? Suggest why different products and brands are distributed through different types of stores.

LO3 **Describe the major types of retail operations.** The major types of retail stores are department stores, specialty retailers, supermarkets, drugstores, convenience stores, discount stores, and restaurants. Department stores carry a wide assortment of shopping and specialty goods, are organized into relatively independent departments, and offset higher prices by emphasizing customer service and decor. Specialty retailers typically carry a narrower but deeper assortment of merchandise, emphasizing distinctive products and a high level of customer service. Supermarkets are large self-service retailers that offer a wide variety of food products and some nonfood items. Drugstores are retail formats that sell mostly prescription and over-the-counter medications, health and beauty aids, cosmetics, and specialty items. Convenience stores carry a limited line of high-turnover convenience goods. Discount stores offer low-priced general merchandise and consist of four types: full-line discounters, specialty discount retailers, warehouse clubs, and off-price retailers. Finally, restaurants straddle the line between the retailing and services industries; although restaurants sell a product, food, and drink to final consumers, they can also be considered service marketers because they provide consumers with the service of preparing food and sometimes table service.

3.1 Discuss the possible marketing implications of the recent trend toward supercenters, which combine a supermarket and a full-line discount store.

3.2 Explain the function of warehouse clubs. Why are they classified as both wholesalers and retailers?

3.3 Would you be interested in buying luxury items, like expensive jewelry, at a warehouse club? Wal-Mart offered a $350,000 diamond solitaire ring during a recent Christmas shopping season. If you could afford such a ring, would you consider buying it at Wal-Mart? Why or why not?

LO4 **Discuss nonstore retailing techniques.** Nonstore retailing, which is shopping outside a store setting, has three major categories. Automatic vending uses machines to offer products for sale. In direct retailing, the sales transaction occurs in a home setting, typically through door-to-door sales or party plan selling. Direct marketing refers to the techniques used to get consumers to buy from their homes or place of business. Those techniques include direct mail, catalogs and mail order, telemarketing, and electronic retailing, such as home shopping channels and online retailing.

ONLINE

4.1 Go to the Gift Center at online wine retailer Wine.com's Web site at **http://www.wine.com.** How does this site help shoppers select gifts?

ONLINE

4.2 How much does the most powerful computer with the fastest modem, most memory, largest monitor, biggest hard drive, and all the available peripherals cost at **http://www.dell.com?** Then visit a store like Best Buy or Circuit City and price a comparable computer. How can you explain any price differences between the two retail operations? Explain any differences in features that you encountered. What conclusions can you draw from your research?

ONLINE

4.3 Most catalog companies also offer online shopping. Visit the Web site of one of your favorite catalogs to see if you can buy online. If so, surf the online catalog for a few minutes. Then compare the two retailing methods (paper and Internet) for prices, products, and so forth. Which do you prefer—the paper catalog or online shopping? Why?

WRITING

4.4 To what can you attribute the renewed interest in the party format of retailing? Go to the library and research direct sales parties. Write a paragraph describing the target market for these parties and the shifts in the external environment that contribute to their resurgent popularity.

LO5 **Define franchising and describe its two basic forms.** Franchising is a continuing relationship in which a franchisor grants to a franchisee the business rights to operate or to sell a product. Modern franchising takes two basic forms. In product and trade name franchising, a dealer agrees to buy or sell certain products or product lines from a particular manufacturer or wholesaler. Business format franchising is an ongoing business relationship in which a franchisee uses a franchisor's name, format, or method of business in return for several types of fees.

5.1 What advantages does franchising provide to franchisors as well as franchisees?

5.2 Curves is the world's largest fitness franchise and was recently the fastest-growing franchise of any kind. What do you need to do to become a Curves franchisee? Visit the Web page **http://www.curves.com** to find out. Does anything surprise you?

LO6

List the major tasks involved in developing a retail marketing strategy. Retail management begins with defining the target market, typically on the basis of demographic, geographic, or psychographic characteristics. After determining the target market, retail managers must develop the six variables of the retailing mix: product, promotion, place, price, presentation, and personnel.

6.1 Identify a successful retail business in your community. What marketing strategies have led to its success?

6.2 How can a company create an atmosphere on its Web site? Visit the pages of some of your favorite retailers to see if they have been able to re-create the store atmosphere on the Internet.

LO7

Describe new developments in retailing. Four major trends are evident in retailing today—interactivity, m-commerce, pop-up shops, and the store-in-a-store model. Adding interactivity to the retail environment is one of the most popular strategies in retailing in recent years. Small retailers as well as national chains are using interactivity to involve customers and set themselves apart from the competition. M-commerce (mobile e-commerce) is gaining in popularity. M-commerce enables consumers to purchase goods and services using wireless mobile devices, such as mobile telephones, pagers, PDAs, and handheld computers. Pop-up shops allow companies flexible locations without the expense of a long-term lease. A store-in-a-store provides shopping convenience.

7.1 Make a list of stores that actively incorporate some kind of interactivity or entertainment into their retailing strategy. Now, make a list of stores that do not, such as office supply stores. Compare your two lists. Select a company from your second list and draft a strategy to help it become more interactive.

7.2 What kind of retailers or brands do you think would most benefit from a pop-up shop? Why?

Key Terms

Exercises

APPLICATION EXERCISE

After reading the chapter, you can see that differences in retailing are the result of strategy. To better understand the relationship between strategic retailing factors and consumer perceptions, you can conduct a simple observation exercise. First, pick a product to shop for, and then identify two stores where you have *never* shopped as places to look for your product. The two stores must be different types of retailers. For example, you can shop for a new HDTV at Best Buy (category killer) and at Hollywood Video (specialty retailer). Once you have identified what you are looking for and where you're going to look, visit each store and record your observations of specific strategic retailing factors.[46]

Activities

1. Go through each store and make careful observations of the following:
   - *Location*: Where is each store? How congested is the area of town where each store is located? What influence does the neighborhood have on your impression of the store? Would you travel to this store under normal circumstances? Write a detailed paragraph on the location of each store.
   - *Exterior atmosphere*: Is there parking? If so, is it convenient? Is it adequate? Observe other parking issues (cleanliness and size of the lot, size of spaces, well-lit, etc.). What kinds of stores are around the store you are visiting? Do you think being located next to them increases traffic at your store? Are direct competitors nearby? Is the building modern or historic? Is it attractive, clean, and appealing? Is the entrance inviting to shoppers?
   - *Interior atmosphere*: Compare the following attributes at each store: aisle width; lighting; number of customers; noise (background music, loudspeakers, etc.); store layout; signage; accessibility of the cashier; number of products available (depth and width of assortment); ability to inspect the product before purchase; quality of the fixtures (shelves, lights, etc.); availability of salespeople and their knowledge about the product; willingness of salespeople to help.
   - *Product*: Is your product available? If not, is there a satisfactory substitute? What is your perception of the quality of goods offered? Why do you think as you do?
   - *Price*: What is the price of the product/brand at this store? Is the price prominently marked? How do the prices at the two stores compare? How does the price compare to your expectations?
2. From which of these two stores would you actually purchase the item? Why, specifically? List the factors that played a role in your decision. Which factor is most important to you? If you would not purchase the item at either store, why not?
3. What are the three most important differences you observed between the stores?
4. Using the results of your research, write a short paper that outlines your observations. Conclude your paper with your answers to questions 2 and 3.

WRITING

ETHICS

ETHICS EXERCISE

A–Z Grocery Company is well known for offering quality grocery products at the lowest prices in the market. When the company applied for a zoning change to build a new store in a middle-class neighborhood, several members of the city council objected because the company has no stores in low-income neighborhoods, where they argue the low prices are needed most. The company contends that it cannot operate profitably in these neighborhoods because of higher security and operating costs.

Questions

1. Should low-cost retailers be required to locate near low-income customers? Why or why not?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketingpower.com** and review the code. Then, write a brief paragraph on how the AMA Statement of Ethics relates to retailing locations.

© AP PHOTO/ELAINE THOMPSON

Case Study: Nordstrom

HOW TO SUCCEED BY SELLING JUST ONE SHOE[47]

Upscale retailer Nordstrom has been famous for superior customer service for over one hundred years. Robert Spector, coauthor of *The Nordstrom Way,* says his favorite story is of a woman with one leg who jokingly bet a Nordstrom salesperson that he wouldn't sell her just one shoe. He was more than happy to split up the pair, though, to her surprise, and Nordstrom gained a life-long customer in the process. "Who knows how many times she's told that story?" Spector asks. "Do you think that that's worth the price of a shoe? I do." This kind of word-of-mouth publicity means that Nordstrom spends much less on traditional advertising than its competitors do. And the stories told by satisfied customers are much more persuasive than an ad in the Sunday paper.

Patrick McCarthy, who was the first salesperson to generate $1 million, cites an example of a customer who was traveling and accidentally left his plane tickets in the store. An employee who found them paid for a cab to the airport with her own money so that the customer wouldn't miss his plane. This, McCarthy says, is an example of "heroic service," and at Nordstrom they expect nothing less.

Industry observer Lior Arussy calls Nordstrom's business strategy "greed through love." They have perfected the art of focusing on the right customers and giving them undivided attention. A salesperson will often continue the relationship with a customer for years. They may exchange business cards, set future shopping dates, and call customers when new merchandise comes in. "It's a heart experience," says McCarthy, who kept handwritten notes on all 12,000 of his personal customers over the years. "Most companies are head experiences—bean counters are running them. When the heart is running them, it becomes exciting."

Nordstrom is also known for its generous exchange policy. In a familiar story that has been forwarded around the Internet for years, a man claims he was allowed to return snow tires, even though the store never sold auto parts. It may be an urban myth, but it reinforces the company's reputation for putting customers first. Even though the company loses some money on returns, they believe it's worth it to keep customers coming back.

Nordstrom has 157 stores in 27 states, but they plan to open 19 more by 2010, expanding into Boston, Ohio, and other untapped U.S. markets. Eric Nordstrom, the company's President, visits each potential location himself before signing off on it. He says his gut instinct about a location is almost as important as the demographics and statistics they analyze. "Plenty of places look good on paper and we say no."

Even though Nordstrom values the traditions that come with its long history, Nordstrom Direct President Jamie Nordstrom says that they're not afraid to evolve with the times. "We see the way people shop changing very dramatically," he says. The company analyzed barriers between its sales channels and realized that it was limiting sales opportunities. Customers who purchased Nordstrom merchandise online couldn't return it in the retail stores, for example, and customers who shopped in the stores couldn't always find the same products online. The company now aims for a "seamless" shopping experience across all sales channels, whether mail order, online, or in-store.

The company has also benefited from a new computerized inventory system that gives buyers and salespeople the necessary data to make smarter decisions about what is needed in the stores—and what isn't. Choosing the right handbags to stock, for example, in the right styles, quantities, and colors, enabled them to sell more items at full price, which in turn improved the bottom line.

Eric Nordstrom says that they want a customer's experience to be "aspirational and upscale, so people feel they are treating themselves." Therefore, he says, the company refuses to hop on the price-promoting bandwagon. "We don't rely on promotions, be it one-day sales, coupons, or 'friends of friends' sales. We think our regular pricing has to have integrity."

In 2006 when many retailers were struggling, Nordstrom thrived, posting $8.6 billion in sales, a 10.8 percent increase from the year before. "We have momentum," Eric Nordstrom says, "but it's not easy sustaining it. Retailing is not for everybody. It's a competitive, high-energy business. Every day, you've got to open your doors and sell something." Even if it's just one shoe.

Questions

1. What type of retailer is Nordstrom? Describe the characteristics it shares with other retailers of this type.
2. How would you describe Nordstrom's level of service on the continuum from full service to self-service? Why? Give an example of a store that would be on the opposite end of the continuum and explain their differences.
3. Which of the six components of Nordstrom's retailing mix do you think have been the most important to the company's success? Why?

4. What are the primary challenges Nordstrom faces in the current retail climate? How has the competition changed in recent years, along with consumer expectations?

Company Clips

SEPHORA—RETAILING FOR SUCCESS

From the beginning, Sephora has carried quality skincare products. Excellent retailing techniques, however, are the real driving force behinds Sephora's success. The company's open-sale environment allows consumers to try any product, or even take home a free sample, before they buy. A great location in the heart of the New York City retail district makes it easy for Sephora to attract potential buyers. Sephora also invests a lot of time and money into training their sales staff so that when customers enter the store, they gain a total shopping experience in which their every need is met. The salespeople are not paid on commission, so they are free to give honest recommendations of products that would be best for their customers. As you watch the video, notice what other retailing methods Sephora uses to promote sales.

Questions

1. Visit **http://www.Sephora.com** and browse the online store. How does Sephora use the online environment to promote its products without the advantage of letting customers try before they buy?
2. Sephora is working out the details of a new loyalty program, and they have asked you to give your input and advice. What do you tell them? How should they integrate this new program with the retailing mix they have already adopted?

Marketing & You Results

If your score was on the low side, it means you don't find shopping in stores to be enjoyable. The higher your score, the more likely you are to think shopping is a fun activity. But beware: a high score can also indicate a tendency toward being a compulsive buyer!

Marketing Miscue

Zune Falters on Valentine's Day Commitment

In late 2006, Microsoft Corporation, the world-wide leader in software, services, and solutions, announced the introduction of its Zune™ line of products. Rather than just a product line, however, Microsoft referred to the Zune offerings as the "Zune Experience." This experience centered on the consumer's ability to connect to share entertainment—connection to a person's music library, connection to friends, connection to the community, and connection to other devices. In a Microsoft press release, the company's VP for Design and Development J. Allard stated, "With Zune, we are not simply delivering a portable device, we are introducing a new platform that helps bring artists closer to their audiences and helps people find new music and develop new social connections."

PR NEWSFOTO/© MICROSOFT CORPORATION

Part of Microsoft's Entertainment and Devices Division, the first Zune release included a 30GB digital media player and the Zune Marketplace music service (the online music subscription costs $14.99 per month). The media player featured wireless technology, a built-in FM transmitter, and a three-inch screen. It was available in black, brown, or white. To enhance and facilitate the Zune experience, every Zune device came preloaded with content from a wide variety of record labels. The product line included three Zune accessory packs (accessory pack items could also be purchased individually): the Zune Car Pack (e.g., charger), the Zune Home A/V Pack (cables, docking station, wireless remote), and the Zune Travel Pack (earphones, remote, gear bag, cable, adapter). Additionally, Zune software for the PC would download updates as Zune evolved through additional product development and enhancements. The Zune device and online service became available to consumers in November of 2006 at a retail price of $249.99.

One year into the product launch, the Zune 4GB and Zune 8GB were offered for $149.99 and $199.99. Available in black, pink, red, and green, the media devices had a 1.8 inch glass screen in addition to all of the other Zune Experience offerings such as the Zune Marketplace and wireless synchronization. Then in January of 2008, Microsoft announced that it would make the Zune 80GB available in red for Valentine's Day. This red wireless digital media player would come with Zune Originals. Zune Originals is the company's online store (**http://zuneoriginals.net**) that allows purchasers to custom-build the device with laser engraved artwork and text on the back of the Zune. At Zune Originals, the buyer had to follow three simple steps: (1) select from the 4GB, 8GB, and 80GB Zune, (2) choose the Zune color, and (3) select the text and/or artwork.

The Valentine's Day option featured artwork from Colorblok, Friends With You, PSYPO, and Studio Play Pretend. Each graphic could be aligned with three lines of text for a personal message to the Valentine's Day recipient. The 80GB red Zune offered a 3.2 inch screen and in-ear noise-isolating headphones along with the traditional Zune offerings of the previous models. The estimated price for the red Zune 80GB was $249.00. Gift-wrapping and shipping were offered at no additional charge as a Valentine's Day special. After purchasing a Zune player for their loved ones, customers could easily load love songs via Zune Marketplace with playlist offerings such as "Hip Hop Valentine," "80s Love," "Broken Love," and other love songs readily available online.

Unfortunately, Microsoft was reported to have begun sending massive e-mails in early February 2008 announcing a delay on the shipment of the red Valentine's Day Zune. One blog quoted the Microsoft e-mail as saying, "Due to some issues in our fulfillment center there remains a chance we will miss getting your Zune to you by February 14^{th}." The company was also refunding the purchase price of the Zune ($249.00), while still promising to ship the Zune once the order fulfillment problem was rectified. The e-mail to customers supposedly went on to read, "We sincerely apologize for not meeting this goal in this specific case. We will be refunding the entire amount of your order, which you should be able to see on your credit/debit card within 7-10 days. We hope you love your Zune and that you will accept our sincere apology."

With less than a week before Valentine's Day, customers who had purchased the Zune as a gift were faced with having to come up with another Valentine's Day gift for their loved one. It remains to be seen whether or not the refund plus the Zune product will rectify this major Valentine's Day distribution faux pas.

Questions

1. What is the channel structure for Zune?
2. Describe the logistical components of this supply chain.

Critical Thinking Case

McDonald's Secret Weapon

Headquartered in Oak Brook, Illinois (USA), McDonald's is the world's largest foodservice retailing chain. The company has over 30,000 restaurants in more than 100 countries. Worldwide, over 50 million people eat McDonald's food daily. Some of the company's most popular menu items are its Big Mac, Quarter Pounder, Chicken McNuggets, Egg McMuffin, and, of course, french fries. Amidst heated public policy debate about fast-food and nutrition, the fast-food leader appears to be accelerating its expansion plans. It is doing so by testing new, healthier products such as more fruit and vegetable side dishes and by expediting the trans-fat-free frying medium oil rollout. Additionally, the company plans to stimulate growth by investing considerably in the global marketplace. Countries in which the company forecasts significant growth potential are China, Russia, France, the United Kingdom, and Australia.

Worldwide, the informal, away-from-home food category in which McDonald's competes is projected to grow by $ 200 billion by the end of 2010. McDonald's plans to garner a significant share of this marketplace growth by increasing the number of restaurants with a 24-hour drive-thru, customizing menus with localized products, and offering meal delivery in its international markets.

By 2008, McDonald's was offering delivery service in 25 cities in 17 countries. According to a McDonald's spokesperson, delivery worked well in very congested cities in which there was a culture of delivery. In these cities, there is not affordable real-estate in which to place a drive-thru window, and there is an abundance of cheap labor to deliver the food to customers. Additionally, unlike McDonald's consumers in the United States, consumers in developing countries are less likely to have automobiles in which to run out to pick up food.

The McDonald's delivery concept was first pioneered in Egypt in 1995. Currently, delivery in Egypt accounts for almost 30 percent of sales (and up to 80 percent in some restaurants). The idea for a delivery service came from its local franchisee a mere one year after McDonald's had entered Egypt. The franchisee realized that other fast-food chains and even five-star hotels offered a delivery option. Two factors were critical to success in Egypt. One, the company had to establish a call center with a toll-free number for metropolitan Cairo. Two, the company had to hire hundreds of scooter drivers to deliver the food products rapidly so that the customer was assured of fresh, hot McDonald's products. More than ten years after pioneering the effort, almost all of the McDonald's restaurants in Cairo offer a delivery service, while only a couple have drive-through windows.

Globally, delivery sales were expected to be around $110 million by 2008, with expected annual growth from 20 to 30 percent annually. This growth rate is more than triple the chain's overall growth rate. Most importantly, delivery is very profitable for a restaurant. The delivery fee runs anywhere from $.50 to $1.00, which covers per-call cost to the call center and delivery costs for the scooter drivers. From a cost perspective, the delivery option actually reduces in-store costs as the restaurants do not incur the associated clean-up costs for eat-in customers. The delivery sale becomes incremental profit for the company.

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As the McDelivery model expands into more and more congested cities in developing countries, the company will have to work closely with the franchisees to maintain quality standards. For example, delivery service in Hyderabad, India, is available to neighborhoods within 10 minutes of the restaurant. The McDelivery service in Singapore offers a website with step-by-step instructions for how to become a registered delivery customer and then to order meals online.

Numerous blogs exist in which residents of the United States express interest in McDelivery. However, the company does not appear to be interested in making the delivery option available in the United States. Yet, one has to wonder if it will take more than a menu change to keep McDonald's competitive in the United States. What might be the company's secret weapon in the United States?

Questions:

1. Who are McDonald's competitors?
2. What is the marketplace profile that fits with McDelivery? Why do locations in the United States not fit this profile?

ANATOMY OF A Store Layout

Grocery

1 If a store wants to project a "service" image as well as "fresh food" image, services are placed near the entrance.

2 Vegetables and fruits are placed near beginning of the store's traffic pattern for their inviting, "fresh food" image.

3 Pharmacy + floral shop + restaurant = scrambled merchandizing.

4 'Race track' arrangement keeps customers moving through the store and making purchases.

7 Reduced service (self bagging and self checkout) saves time and reduces costs.

5 Staples such as meat, eggs, milk, and bakery items are placed farthest from the entrance because the more products a shopper passes by, the more they are likely to purchase.

6 Food manufacturers pay "slotting" fees to get aisle end caps and eye-level shelf space. Upper- and lower-level shelf space is reserved for low-margin/low-profit items.

PART 5

Promotion *and* Communication Strategies

WHAT'S INSIDE

Promotional Planning for Competitive Advantage

CHAPTER

16

Learning Outcomes

- LO 1 Discuss the role of promotion in the marketing mix
- LO 2 Describe the communication process
- LO 3 Explain the goals of promotion
- LO 4 Discuss the elements of the promotional mix
- LO 5 Discuss the AIDA concept and its relationship to the promotional mix
- LO 6 Discuss the concept of integrated marketing communications
- LO 7 Describe the factors that affect the promotional mix

LO 1

The Role of Promotion in the Marketing Mix

promotion
Communication by marketers that informs, persuades, and reminds potential buyers of a product in order to influence an opinion or elicit a response.

promotional strategy
A plan for the optimal use of the elements of promotion: advertising, public relations, personal selling, and sales promotion.

competitive advantage
One or more unique aspects of an organization that cause target consumers to patronize that firm rather than competitors.

Few goods or services, no matter how well developed, priced, or distributed, can survive in the marketplace without effective **promotion**—communication by marketers that informs, persuades, and reminds potential buyers of a product in order to influence their opinion or elicit a response.

Promotional strategy is a plan for the optimal use of the promotional mix elements: advertising, public relations, personal selling, and sales promotion. As Exhibit 16.1 shows, the marketing manager determines the goals of the company's promotional strategy in light of the firm's overall goals for the marketing mix—product, place (distribution), promotion, and price. Using these overall goals, marketers combine the elements of the promotional mix into a coordinated plan. This promotional plan defines the promotional strategy, which then becomes an integral part of the overall marketing strategy for reaching the target market.

The main function of a marketer's promotional strategy is to convince target customers that the goods and services offered provide a competitive advantage over the competition. A **competitive advantage** is the set of unique features of a company and its products that are perceived by the target market as significant and superior to the competition. Such features can include high product quality, rapid delivery, low prices, excellent service, or a feature not offered by the competition. For example, fast-food restaurant Subway promises fresh sandwiches that are better for you than a hamburger or pizza. Subway effectively communicates its competitive

Marketing & You

Using the following scale, enter your opinions on the lines provided.

1	2	3	4	5	6
Strongly disagree					Strongly agree

— People frequently tell me about themselves.

— I've been told that I'm a good listener.

— I'm very accepting of others.

— People trust me with their secrets.

— I easily get people to "open up."

— People feel relaxed around me.

— I enjoy listening to people.

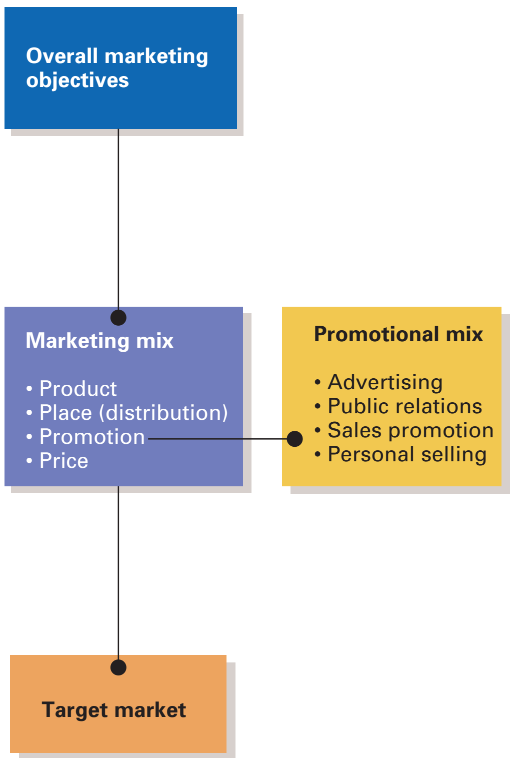
— I'm sympathetic to people's problems.

— I encourage people to tell me how they are feeling.

— I can keep people talking about themselves.

Total your score, and see what it means after you read the chapter.

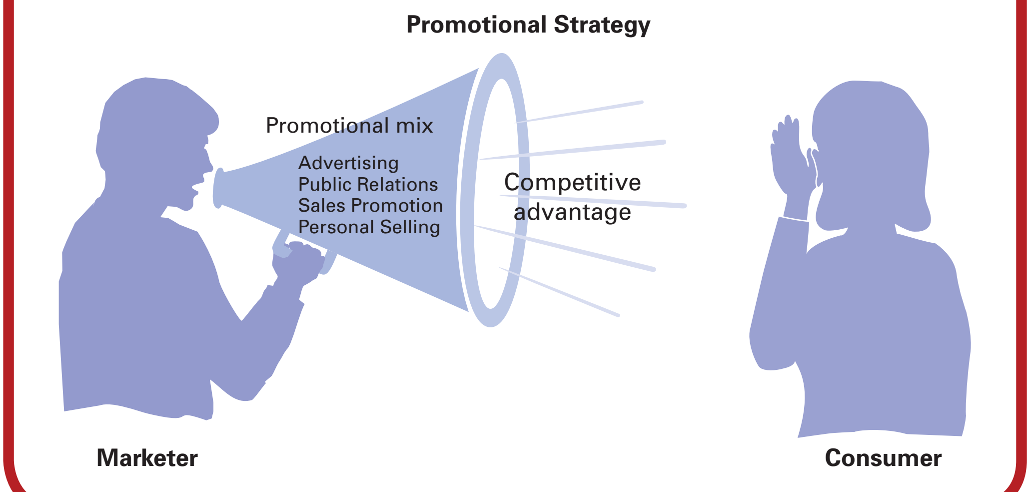
Exhibit 16.1
Role of Promotion in the Marketing Mix



advantage through advertising featuring longtime "spokes-eater" Jared Fogle, who lost weight by eating at Subway every day.[1] Thus, promotion is a vital part of the marketing mix, informing consumers of a product's benefits and thereby positioning the product in the marketplace.

REVIEW LEARNING OUTCOME

LO 1 Discuss the role of promotion in the marketing mix



LO 2
Marketing Communication

communication The process by which we exchange or share meanings through a common set of symbols.

interpersonal communication Direct, face-to-face communication between two or more people.

mass communication The communication of a concept or message to large audiences.

Promotional strategy is closely related to the process of communication. As humans, we assign meaning to feelings, ideas, facts, attitudes, and emotions. Communication is the process by which we exchange or share meanings through a common set of symbols. When a company develops a new product, changes an old one, or simply tries to increase sales of an existing good or service, it must communicate its selling message to potential customers. Marketers communicate information about the firm and its products to the target market and various publics through its promotion programs. When Sara Lee Corp. decided to re-invigorate its legacy brand, Kiwi shoe polish, it began with communication: it asked people about their shoe care needs. After interviewing 3,500 people across eight countries, it found out that people cared more about fresh, comfortable shoes than whether those shoes were polished. Sara Lee's new CEO welcomes innovation. She found out which innovations would be welcome by communicating with Kiwi's consumers, marketers, and retailers, then she pushed the employees to "think outside the box—or inside the shoe," and it paid off. Kiwi's new products—including thin insoles with built-in fresheners and single-use polishes—pushed Kiwi's sales up (for the first time in a long time) by 4.4 percent in 2007. Now Sara Lee is using that same innovation-driven-by-communication model and holding focus groups with its employees and customers to find out which new products will revive Sara Lee's other brands.[2]

Communication can be divided into two major categories: interpersonal communication and mass communication. Interpersonal communication is direct, face-to-face communication between two or more people. When communicating face-to-face, people see the other person's reaction and can respond almost immediately. A salesperson speaking directly with a client is an example of an interpersonal marketing communication. Mass communication involves communicating a concept or message to large audiences. A great deal of marketing communication is directed to consumers as a whole, usually through a mass medium such as television or newspapers. When a company advertises, it generally does not personally know the people with whom it is trying to communicate. Furthermore, the company is unable to respond immediately to consumers' reactions to its message. Instead, the marketing manager must wait to see whether people are reacting positively or negatively to the mass-communicated promotion. Any clutter from competitors' messages or other distractions in the environment can reduce the effectiveness of the mass-communication effort.

THE COMMUNICATION PROCESS

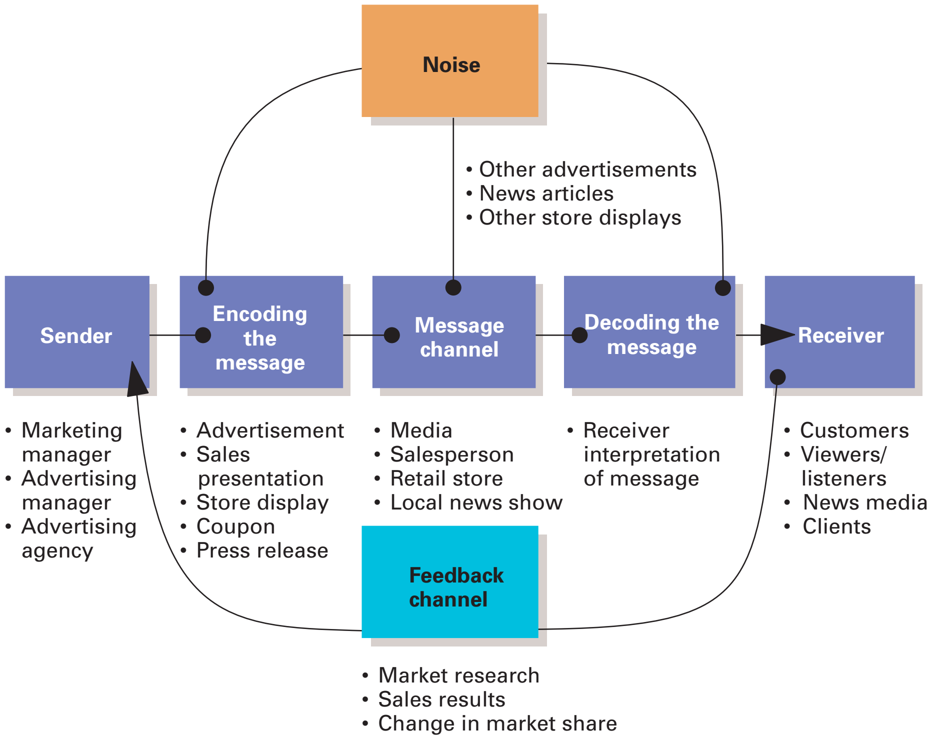
Marketers are both senders and receivers of messages. As *senders,* marketers attempt to inform, persuade, and remind the target market to adopt courses of action compatible with the need to promote the purchase of goods and services. As *receivers,* marketers attune themselves to the target market in order to develop the appropriate messages, adapt existing messages, and spot new communication opportunities. In this way, marketing communication is a two-way, rather than one-way, process. The two-way nature of the communication process is shown in Exhibit 16.2.

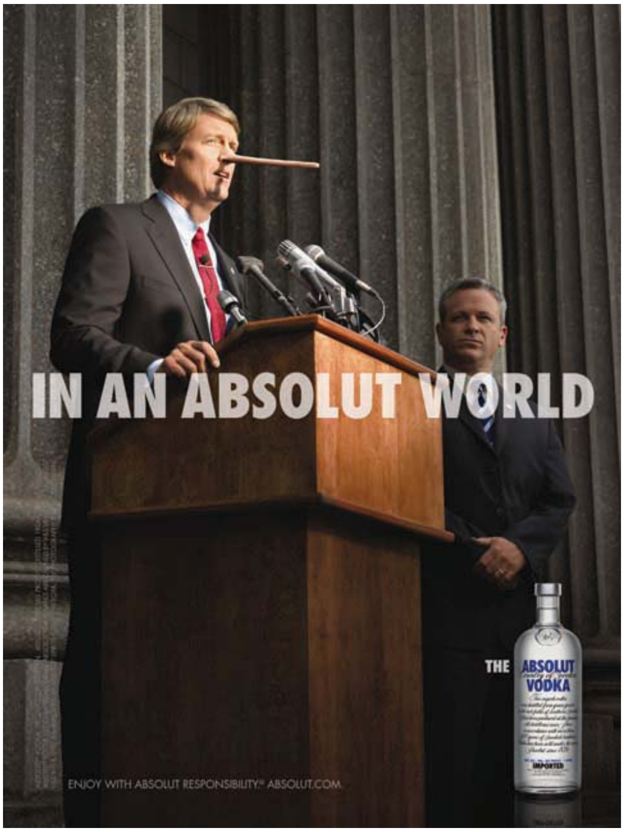
The Sender and Encoding

sender
The originator of the message in the communication process.

The **sender** is the originator of the message in the communication process. In an interpersonal conversation, the sender may be a parent, a friend, or a salesperson. For an advertisement or press release, the sender is the company or organization itself. For example, the Swedish brand Absolut Vodka launched a marketing campaign using the theme "In an Absolut World." At the outset, the objective of the campaign was to increase Absolut's market share in the crowded and increasingly competitive U.S. vodka market. To appeal to this market, Absolut had to differentiate its message from the "rational benefits" (such as best taste or smooth feel) being claimed by so many of the upstarts in the vodka category. Absolut changed

Exhibit 16.2
Communication Process





UNDER PERMISSION BY V&S VIN & SPRIT AB

its near-legendary superpremium brand strategy—a print campaign pairing the iconic shape of its bottle with equally iconic art figures—to a campaign that would appeal to the "emotional benefits" of the brand.[3] Thus,

Absolut launched a new campaign using the phrase "Absolut World" to promote the message that their vodka was the brand to choose if the customer was intelligent, savvy, and wanted to challenge the status quo by taking on bold and optimistic new world views. The new ads assert that Absolut vodka is in a class by itself indeed, in a world of its own, an "Absolut World."[4] The ad campaign also invites Absolut's consumers to visualize a world that appeals to them—even a world that may be idealized or "fantastic."[5]

Encoding is the conversion of the sender's ideas and thoughts into a message, usually in the form of words or signs. A basic principle of encoding is that what matters is not what the source says but what the receiver hears. One way of conveying a message that the receiver will hear properly is to use concrete words and pictures. For example, Absolut's marketers encoded the message by a creating a series of life-size outdoor ads, TV commercials, wrapped buildings, and other media that imagined an "Absolut World" where factories emit harmless bubbles instead of smoke, ATMs dispense "free" money, politicians' noses grow if they lie, and people in bars wear buttons labeling their dating status and mindset.[6]

encoding
The conversion of a sender's ideas and thoughts into a message, usually in the form of words or signs.

channel
A medium of communication—such as a voice, radio, or newspaper—for transmitting a message.

noise
Anything that interferes with, distorts, or slows down the transmission of information.

receiver
The person who decodes a message.

decoding
Interpretation of the language and symbols sent by the source through a channel.

Message Transmission

Transmission of a message requires a channel—a voice, radio, newspaper, or other communication medium. A facial expression or gesture can also serve as a channel.

Reception occurs when the message is detected by the receiver and enters his or her frame of reference. In a two-way conversation such as a sales pitch given by a sales representative to a potential client, reception is normally high. In contrast, the desired receivers may or may not detect the message when it is mass communicated because most media are cluttered by noise—anything that interferes with, distorts, or slows down the transmission of information. In some media overcrowded with advertisers, such as newspapers and television, the noise level is high and the reception level is low. For example, competing network advertisements, other entertainment option advertisements, or other programming on the network itself might hamper reception of the "Absolut World" advertising campaign message. Transmission can also be hindered by situational factors such as physical surroundings like light, sound, location, and weather; the presence of other people; or the temporary moods consumers might bring to the situation. Mass communication may not even reach all the right consumers. Some members of the target audience were likely watching television when Absolut's commercials were shown, but others probably were not.

The Receiver and Decoding

Marketers communicate their message through a channel to customers, or receivers, who will decode the message. Decoding is the interpretation of the language and symbols sent by the source through a channel. Common understanding between two communicators, or a common frame of reference, is required for effective communication. Therefore, marketing managers must ensure a proper match between the message to be conveyed and the target market's attitudes and ideas.

Even though a message has been received, it will not necessarily be properly decoded—or even seen, viewed, or heard—because of selective exposure, distortion, and retention (refer to Chapter 6). Even when people receive a message, they tend to manipulate, alter, and modify it to reflect their own biases, needs, knowledge, and culture. Differences in age, social class, education, culture, and ethnicity can lead to miscommunication, for example. Further, because people don't always listen or read carefully, they can easily misinterpret what is said or written. In fact, researchers have found that consumers misunderstand a large proportion of both printed and televised communications. Bright colors and bold graphics have been shown to increase consumers' comprehension of marketing communication. Even these techniques are not foolproof, however. A classic example of miscommunication occurred when Lever Brothers mailed out samples of its then new dishwashing liquid, Sunlight, which contains real lemon juice. The package clearly stated that Sunlight was a household cleaning product. Nevertheless, many people saw the word *sunlight,* the large picture of lemons, and the phrase "with real lemon juice" and thought the product was lemon juice.

Marketers targeting consumers in foreign countries must also worry about the translation and possible miscommunication of their promotional messages by other cultures. An important issue for global marketers is whether to standardize or customize the message for each global market in which they sell. While Absolut's marketers used the "World" message globally, they tailored the ads to reflect how people in various regions might envision an "Absolute World." For example, a bus shelter on 2nd Avenue in New York City was wrapped to look like a subway entrance—a dream of many New York commuters. In Germany, consumers were given a first-hand experience of the "Absolut World." For one week, a fleet of Porsche taxis chauffeured passengers quickly—and for free—around Hamburg, Munich, and Berlin. By the end of that week, the taxis had generated over 15 million media contacts through TV, print, and online news coverage.[7]

Feedback

feedback
The receiver's response to a message.

In interpersonal communication, the receiver's response to a message is direct feedback to the source. Feedback may be verbal, as in saying "I agree," or nonverbal, as in nodding, smiling, frowning, or gesturing.

Because mass communicators like Absolut's are often cut off from direct feedback, they must rely on market research or analysis of viewer responses for indirect feedback. Absolut might use such measurements as the percentage of television viewers who recognized, recalled, or stated that they were exposed to Absolut's messages. Indirect feedback enables mass communicators to decide whether to continue, modify, or drop a message.

THE IMPACT OF BLOGGING ON MARKETING COMMUNICATION

The Internet and related technologies are having a profound impact on marketing communication. The rise of blogging, for example, has created a completely new way for marketers to manage their image, connect with consumers, and generate interest in and desire for their companies' products.

Despite what could be considered a national obsession with blogs, measuring blogging activity remains challenging. According to Technorati, the first blog search engine, there were 28.4 million blogs online in 2006. By early 2008, Technorati was tracking 112.8 million blogs.[8] In spite of the widespread popularity of blogging, a blog's life expectancy is short. Fewer than half of all blogs are receiving posts three months after their creation, and less than 10 percent are updated as often as weekly.[9] Moreover, a Gallup poll found that only 9 percent of Internet users read blogs frequently, 24 percent read them occasionally or less, and nearly 66 percent are not involved in blogging at all.[10]

The question then is whether blogging is a passing fad, representing at best an unreliable means of communicating, or an emerging trend. If it is a fad, why are marketers so interested in blogging as a promotional tool? The answer in part is

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that blogging alters the marketing communication process for the promotional elements that rely on mass communication—advertising, public relations, and sales promotion—by moving them away from impersonal, indirect communication toward a personalized, direct communication model.

Blogs can be divided into two broad categories: corporate blogs and noncorporate blogs. Corporate blogs are sponsored by a company or one of its brands and maintained by one or more of the company's employees. Corporate blogs disseminate marketing-controlled information. (Recall from Chapter 6 that marketing-controlled information is a source of product information that originates with marketers promoting the product.) Because blogs are designed to change daily, corporate blogs are dynamic and highly flexible, giving marketers the opportunity to adapt their messages more frequently than with any other communication channel. Initially, blogs were maintained by only the most technology-savvy companies. But today companies as diverse as Coca-Cola, Starwood Hotels, Honda, Nokia, Benetton, Ducati, Guinness, and HSBC have all launched corporate blogs. Undoubtedly, many more will appear in the near future.

In contrast, noncorporate blogs are independent and not associated with the marketing efforts of any particular company or brand. As such, noncorporate blogs function much like nonmarketing-controlled information: they provide a source of information and opinion perceived to be independent and more authentic than a corporate blog. Michael Marx loves Barq's root beer. He wears Barq's T-shirts, brings the beverage to parties, and calls it his "beer." He maintains a blog dedicated to Barq's, **http://www.thebarqsman.com**, where he collects news about the brand, Barq's commercials he likes, and musings on why Barq's is superior to other root beers. Thebarqsman.com is not affiliated with Coca-Cola, the owner of the Barq's brand, which had no idea of the blog's existence until a *New York Times* reporter writing a story on brand blogs mentioned it. Even though thebarqsman.com is dedicated to a single brand, Marx's blog is an example of a noncorporate blog.[11]

corporate blogs
Blogs that are sponsored by a company or one of its brands and maintained by one or more of the company's employees.

noncorporate blogs
Independent blogs that are not associated with the marketing efforts of any particular company or brand.

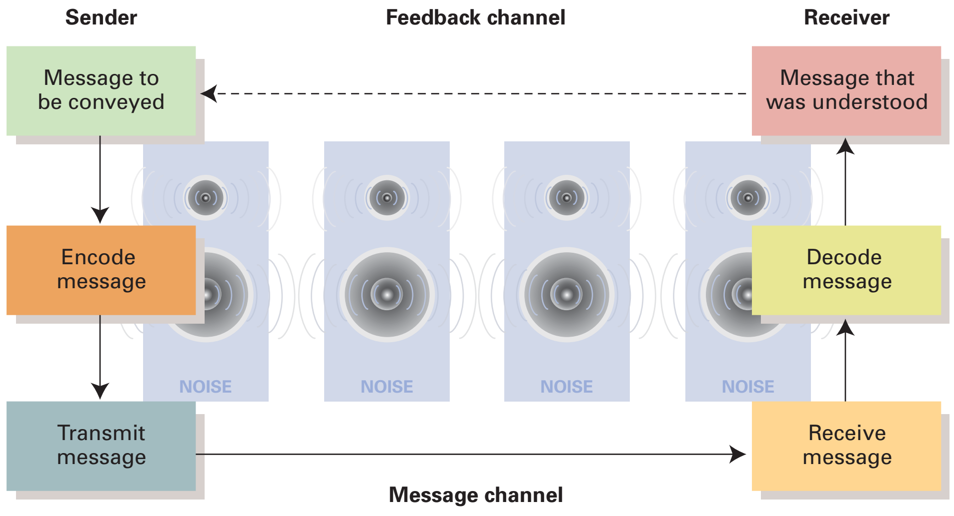
Both corporate and noncorporate blogs have had an impact on the communication model depicted in Exhibit 16.2. That model shows the feedback channel as primarily impersonal and numbers-driven. In the traditional communication process, marketers can see the results of consumer behavior (e.g., a drop in sales), but are only able to explain them using their judgment. Even the information generated by market research is not as natural as that gleaned from bloggers. Corporate blogs allow marketers to personalize the feedback channel by opening the door for direct conversation with consumers.

When marketers launch a corporate blog, they create an unfiltered feedback channel. In 2006 Enrico Minoli, CEO of Ducati, the Italian motorcycle brand, launched a blog at **http://blog.ducati.com**. He vowed to write "openly about what's going on at Ducati." Within three days, his postings had generated 99 responses, from motorcycle enthusiasts from Greece to Daytona Beach, who all seemed most pleased that the CEO himself was a motorbike enthusiast. They began peppering him with questions about when new models would hit production and chatted with each other about their own bikes and biking experiences. Minoli's blog put a face on the impersonal nature of a large corporation.[12]

Noncorporate blogs have also personalized the feedback channel. But while corporate blogs create a *direct*, personalized feedback channel for masses of consumers, noncorporate blogs represent an *indirect,* personalized feedback channel. Because noncorporate blogs are independent, they are often perceived as more authentic. Blogging experts offer marketers some solid advice for giving their blogs the honest quality many bloggers associate with noncorporate blogs: open the feedback channel. Todd Copilevitz, a consultant specializing in digital marketing, says, "Blogs are not an environment where you just hold forth opinion and don't accept feedback. You have to have your wits about you to understand it's not the same old PR machine."[13]

REVIEW LEARNING OUTCOME

LO 2 Describe the communication process



LO 3

The Goals of Promotion

People communicate with one another for many reasons. They seek amusement, ask for help, give assistance or instructions, provide information, and express ideas and thoughts. Promotion, on the other hand, seeks to modify behavior and thoughts in some way. For example, promoters may try to persuade consumers to drink Pepsi rather than Coke, or to eat at Burger King instead of McDonald's. Promotion also strives to reinforce existing behavior—for instance, getting consumers to continue dining at Burger King once they have switched. The source (the seller) hopes to project a favorable image or to motivate purchase of the com pany's goods and services.

Effective promotion will achieve one or more of three goals: It will *inform* the target audience, *persuade* the target audience, or *remind* the target audience. Often a marketer will try to achieve two or more of these goals at the same time.

INFORMING

Informative promotion seeks to convert an existing need into a want or to stimulate interest in a new product. It is generally more prevalent during the early stages of the product life cycle. People typically will not buy a product or service or support a nonprofit organization until they know its purpose and its benefits to them. Informative messages are important for promoting complex and technical products such as automobiles, computers, and investment services. For example, Philips's original advertisement for the Magnavox flat-screen television showed young, urban consumers trying the flat-screen TV all over the house, including the ceiling. The ad focused on "how to" use the flat-screen TV rather than the Philips Magnavox brand or the technological capabilities.[14] Informative promotion is also important for a "new" brand being introduced into an "old" product class—for example, a new brand of frozen pizza entering the frozen pizza industry, which

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is dominated by well-known brands like Kraft's DiGiorno and Schwan's Grocery Products' Red Baron. The new product cannot establish itself against more mature products unless potential buyers are aware of it, value its benefits, and understand its positioning in the marketplace.

PERSUADING

Persuasive promotion is designed to stimulate a purchase or an action—for example, to eat more Doritos or use Verizon wireless mobile phone service. Persuasion normally becomes the main promotion goal when the product enters the growth stage of its life cycle. By this time, the target market should have general product awareness and some knowledge of how the product can fulfill their wants. Therefore, the promotional goal switches from informing consumers about the product category to persuading them to buy the company's brand rather than the competitor's. At this time, the promotional message emphasizes the product's real and perceived competitive advantages, often appealing to emotional needs such as love, belonging, self-esteem, and ego satisfaction. For example, the latest advertisement for the Philips Magnavox flat-screen television still features young, urban consumers. But the ad focuses on the product's benefits such as lifestyle enhancements, technological features like HDTV and Dolby digital surround sound, and the superiority of the brand.[15]

Persuasion can also be an important goal for very competitive mature product categories such as many household items, soft drinks, beer, and banking services. In a marketplace characterized by many competitors, the promotional message often encourages brand switching and aims to convert some buyers into loyal users. For example, to persuade new customers to switch their checking accounts, a bank's marketing manager may offer a year's worth of free checks with no fees.

promotional mix
The combination of promotional tools—including advertising, public relations, personal selling, and sales promotion—used to reach the target market and fulfill the organization's overall goals.

Critics believe that some promotional messages and techniques can be too persuasive, causing consumers to buy products and services they really don't need.

REMINDING

Reminder promotion is used to keep the product and brand name in the public's mind. This type of promotion prevails during the maturity stage of the life cycle. It assumes that the target market has already been persuaded of the good's or service's merits. Its purpose is simply to trigger a memory. Crest toothpaste, Tide laundry detergent, Miller beer, and many other consumer products often use reminder promotion. Similarly, Philips Magnavox could advertise just the brand rather than the benefits of the product.

REVIEW LEARNING OUTCOME

LO3 Explain the goals of promotion

- **Informative promotion**

  Increasing the awareness of a new brand, product class, or product attribute

  Explaining how the product works

  Suggesting new uses for a product

  Building a company image
- **Persuasive promotion**

  Encouraging brand switching

  Changing customers' perceptions of product attributes

  Influencing customers to buy now

  Persuading customers to call
- **Reminder promotion**

  Reminding consumers that the product may be needed in the near future

  Reminding consumers where to buy the product

  Maintaining consumer awareness

LO4 The Promotional Mix

As you read earlier, most promotional strategies use several elements or tools—which may include advertising, public relations, sales promotion, and personal selling—to reach a target market. That combination is called the promotional mix. The proper promotional mix is the one that management believes will meet the needs of the target market and fulfill the organization's overall goals. The more funds allocated to each promotional element and the more managerial emphasis placed on each technique, the more important that element is thought to be in the overall mix.

ADVERTISING

Almost all companies selling a good or a service use some advertising, whether in the form of a multimillion-dollar campaign or a simple classified ad in a newspaper. *Advertising* is any form of impersonal (one-way) paid communication in which the sponsor or company is identified. One of the primary benefits of advertising is its ability to communicate to a large number of people at one time. Traditional media—such as television, radio, newspapers, magazines, books, direct mail, billboards, and transit cards (advertisements on buses and taxis and at bus stops)—are most commonly used to transmit advertisements to consumers. With the increasing fragmentation of traditional media choices, marketers are using relatively new methods to send their advertisements to consumers, such as Web sites, e-mail, and interactive video technology located in department stores and supermarkets. However, as the Internet becomes a more vital component of many companies' promotion and marketing mix, consumers and lawmakers are increasingly concerned about possible violations of consumers' privacy. Read more about this issue in the "Ethics in Marketing" box. Advertising is examined further in Chapter 17.

PUBLIC RELATIONS

Concerned about how they are perceived by their target markets, organizations often spend large sums to build a positive public image. *Public relations* is the marketing function that evaluates public attitudes, identifies areas within the organization the public may be interested in, and executes a program of action to earn public

ETHICS in Marketing

Can E-mail Marketing Survive Anti-Spam Legislation?

Any American who logs onto the Internet is familiar with the ever-present spam filling our in-boxes in the form of e-mails offering herbal supplements, prescription drugs, low-interest loans, investment opportunities, free money, and other products. The term *spam*, the name for unwanted e-mails, comes from a Monty Python skit in which a customer is urged to order Spam (the canned meat product) repeatedly until she screams "I don't want any Spam!"—which is how most of us feel today about the useless products and "phishing" scams we get in our e-mail. Spam raises serious moral issues, especially when it exposes children to pornography and vulnerable people to scams.

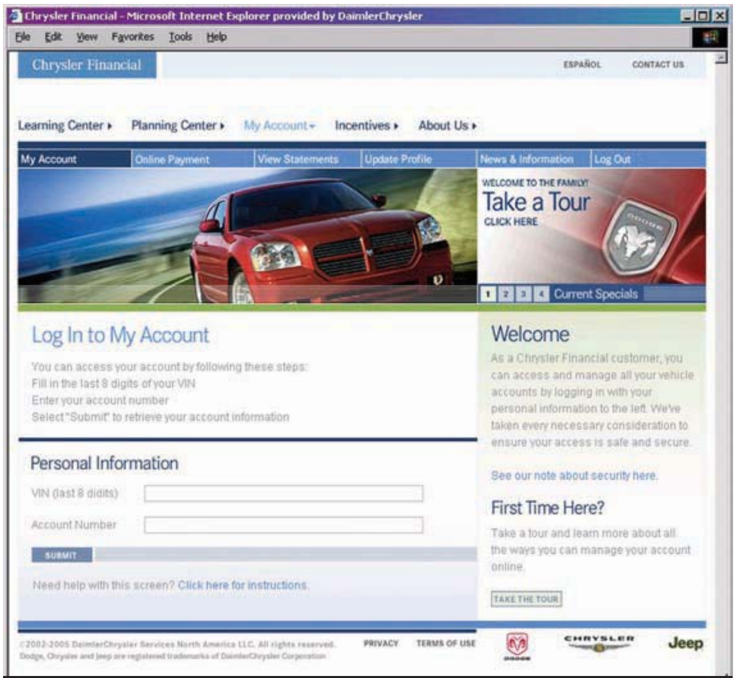
In an effort to curtail the flood of unsolicited commercial e-mails, Congress passed legislation that made it illegal for marketers to send unsolicited commercial e-mails using a false return address or subject line that conceals their identity and to harvest addresses from Web sites. In addition, e-mails are required to have a functioning opt-out mechanism that recipients can use to prevent future e-mails. Marketers who fail to comply can be sentenced to prison for up to five years.

The law curtailed some spamming, but 70 percent of the world's e-mail messages continue to be spam because so much spam originates outside the United States. Also, it is impossible to monitor the effectiveness of the required "opt-out" mechanisms. Although many companies include this option, it often does not work, even when the sender is a supposedly reputable firm. Officials at the Federal Trade Commission claim that the number of spam e-mails is leveling off and say that is evidence the law is working. In addition, the feds are hoping the guilty plea of the defendant in the first case prosecuted under the new anti-spam legislation will further discourage spam.

Spam is a serious problem for e-mail marketers. Consumers consider anything that doesn't interest them to be spam. But legally e-mail isn't spam if a consumer has opted-in to receive messages, and many consumers often forget they opted-in with a particular company. The problem is that if enough consumers claim a message is spam, Internet service providers will classify the marketer as a spammer and start blocking its message.

In spite of these problems, the news isn't all bad for e-mail marketers. About half of consumers take advantage of offers that arrive via e-mail. The number is up significantly in recent years. Discounts, markdowns, and free shipping offers persuade consumers to open messages, and the more messages opened, the more sales are made.[16]

Do you think spam or unsolicited commercial e-mail is an effective marketing tool? When does e-mail become spamming? Can spam be prevented?



PR NEWSFOTO/© CHRYSLER FINANCIAL

The U.S. auto industry is so competitive that domestic firms are struggling to survive. Chrysler, however is finding successful ways to connect with its customers, from the "tell us what you want" page on its Web site, to its Yahoo! Group forums, where owners of Chrysler vehicles and potential buyers can share information about maintenance, common problems, performance improvements, etc.

understanding and acceptance. Public relations helps an organization communicate with its customers, suppliers, stockholders, government officials, employees, and the community in which it operates. Marketers use public relations not only to maintain a positive image but also to educate the public about the company's goals and objectives, introduce new products, and help support the sales effort. Public relations will be covered in more depth in Chapter 17.

PERSONAL SELLING

Personal selling is a purchase situation involving a personal, paid-for communication between two people in an attempt to influence each other. Traditional methods of personal selling include a planned presentation to one or more prospective buyers for the purpose of making a sale. More current notions on personal selling emphasize the relationship that develops between a salesperson and a buyer. Recently, both business-to-business and business-to-consumer selling focus on building long-term relationships rather than on making a onetime sale.

Personal selling, like other promotional mix elements, is increasingly dependent on the Internet. Most companies use their Web sites to attract potential buyers seeking information on products and services. While some companies sell products direct to consumers online, many do not. Instead, they rely on the Web site to drive customers to their physical locations where personal selling can close the sale. Whether it takes place face-to-face, over the phone, or online, personal selling attempts to persuade the buyer to accept a point of view or take some action. Personal selling is discussed further in Chapter 18.

SALES PROMOTION

Sales promotion consists of all marketing activities—other than personal selling, advertising, and public relations—that stimulate consumer purchasing and dealer effectiveness. Sales promotion is generally a short-run tool used to stimulate immediate increases in demand. In fact, marketers often use sales promotion to improve the effectiveness of other ingredients in the promotional mix, especially advertising and personal selling. Research shows that sales promotion complements advertising by yielding faster sales responses. Sales promotion can be aimed at end consumers, trade customers, or a company's employees. Sales promotions include free samples, contests, premiums, trade shows, vacation giveaways, and coupons. A major promotional campaign might use several of these sales promotion tools. Sales promotion is discussed in more detail in Chapter 18.

THE COMMUNICATION PROCESS AND THE PROMOTIONAL MIX

The four elements of the promotional mix differ in their ability to affect the target audience. For instance, promotional mix elements may communicate with the consumer directly or indirectly. The message may flow one way or two ways. Feedback may be fast or slow, a little or a lot. Likewise, the communicator may have varying

Exhibit 16.3

Characteristics of the Elements in the Promotional Mix

	Advertising	Public Relations	Sales Promotion	Personal Selling
Mode of Communication	Indirect and impersonal	Usually indirect and impersonal	Usually indirect and impersonal	Direct and face-to-face
Communicator Control over Situation	Low	Moderate to low	Moderate to low	High
Amount of Feedback	Little	Little	Little to moderate	Much
Speed of Feedback	Delayed	Delayed	Varies	Immediate
Direction of Message Flow	One-way	One-way	Mostly one-way	Two-way
Control over Message Content	Yes	No	Yes	Yes
Identification of Sponsor	Yes	No	Yes	Yes
Speed in Reaching Large Audience	Fast	Usually fast	Fast	Slow
Message Flexibility	Same message to all audiences	Usually no direct control over message	Same message to varied target audiences	Tailored to prospective buyer

degrees of control over message delivery, content, and flexibility. Exhibit 16.3 outlines differences among the promotional mix elements with respect to mode of communication, marketer's control over the communication process, amount and speed of feedback, direction of message flow, marketer's control over the message, identification of the sender, speed in reaching large audiences, and message flexibility.

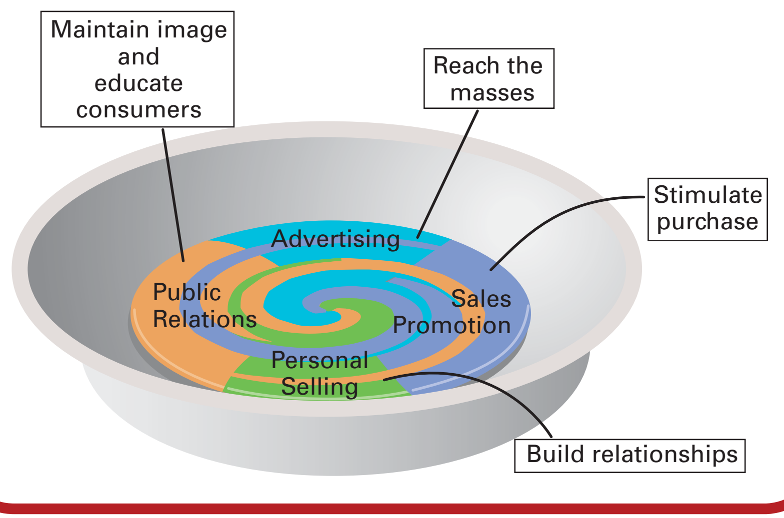
From Exhibit 16.3, you can see that most elements of the promotional mix are indirect and impersonal when used to communicate with a target market, providing only one direction of message flow. For example, advertising, public relations, and sales promotion are generally impersonal, one-way means of mass communication. Because they provide no opportunity for direct feedback, it is more difficult to adapt these promotional elements to changing consumer preferences, individual differences, and personal goals.

AIDA concept
A model that outlines the process for achieving promotional goals in terms of stages of consumer involvement with the message; the acronym stands for attention, interest, desire, and action.

Personal selling, on the other hand, is personal, two-way communication. The salesperson receives immediate feedback from the consumer and can adjust the message in response. Personal selling, however, is very slow in dispersing the marketer's message to large audiences. Because a salesperson can only communicate to one person or a small group of persons at one time, it is a poor choice if the marketer wants to send a message to many potential buyers.

REVIEW LEARNING OUTCOME

LO4 Discuss the elements of the promotional mix



LO5 Promotional Goals and the AIDA Concept

The ultimate goal of any promotion is to get someone to buy a good or service or, in the case of nonprofit organizations, to take some action (for instance, donate blood). A classic model for reaching promotional goals is called the AIDA concept.[17] The acronym stands for *attention, interest, desire,* and *action*—the stages of consumer involvement with a promotional message.

PR NEWSFOTO/© JOHANSEN KRAUSE/APPLE COMPUTER, INC.

This model proposes that consumers respond to marketing messages in a cognitive (thinking), affective (feeling), and conative (doing) sequence. First, a promotion manager may focus on attracting a person's *attention* by training a salesperson to use a friendly greeting and approach, or by using loud volume, unusual color contrasts, bold headlines, movement, bright colors, and the like in an advertisement. Next, a good sales presentation, demonstration, or advertisement creates *interest* in the product and then, by illustrating how the product's features will satisfy the consumer's needs, arouses *desire*. Finally, a special offer or a strong closing sales pitch may be used to obtain purchase *action*.

The AIDA concept assumes that promotion propels consumers along the following four steps in the purchase-decision process:

1. *Attention:* The advertiser must first gain the attention of the target market. A firm cannot sell something if the market does not know that the good or service exists. When Apple introduced the iPod, it was a new product for the company. To create awareness and gain attention for the new product, Apple had to advertise and promote it extensively through ads on TV, in magazines, and on the Internet. Because the iPod was a brand extension of the Apple computer, it required less effort than if it had been an entirely new brand. At the same time, because the iPod was an innovative new product line, the promotion had to get customers' attention and create awareness of a new idea from an established company.
2. *Interest:* Simple awareness of a brand seldom leads to a sale. The next step is to create interest in the product. A print ad or TV commercial cannot tell potential customers all the features and benefits of the iPod. Thus, Apple had to arrange iPod demonstrations and target messages to innovators and early adopters to create interest in the new portable music players.
3. *Desire:* Potential customers for the Apple iPod may like the concept of a portable music player, but they may not feel it is necessarily better than a Sony Walkman portable radio or a portable music player with fewer features. Therefore, Apple had to create brand preference with its iTunes Music Store, extended-life battery, clock and alarm, calendar and to-do list, photo storage, and other features. Specifically, Apple had to convince potential customers that the iPod was the best solution to meet their desire for a portable digital music player.
4. *Action:* Some potential target market customers may have been convinced to buy an iPod but had not yet made the actual purchase. To motivate them to take action, Apple continued advertising to more effectively communicate the features and benefits and also used promotions and price discounts.

Following the initial success of the iPod, to continue its market dominance of the portable digital music player market, Apple introduced new models such as the Nano and Shuffle that were smaller and lighter and yet had longer battery life and more storage. Then podcasting and video were added with access to thousands of network and cable shows and interfaces with auto, boat and home equipment—and the iPod became a "portable media player."

With each product innovation, the cycle of attention, interest, desire, and action began again. But with the familiarity and success of earlier models, the time frame became shorter. In fact, during the Christmas season in 2005, Apple was selling more than 100 iPods per minute; by mid-2007 it had sold 100 million iPods. Moreover, Apple's iTunes Store now sells more music than any other retailer in the US except for Wal-Mart—more than 4 billion songs to over 50 million customers.[18]

Most buyers involved in high-involvement purchase situations pass through the four stages of the AIDA model on the way to making a purchase. The promoter's task is to determine where on the purchase ladder most of the target consumers are located and design a promotion plan to meet their needs. For instance, if Apple learned from its market research that many potential customers were in the desire stage but had not bought an iPod for some reason, then Apple could place advertising on Yahoo or Google, and perhaps in video games as well, to target younger individuals who are the primary target market with specific messages to motivate them to take immediate action and buy an iPod.

The AIDA concept does not explain how all promotions influence purchase decisions. The model suggests that promotional effectiveness can be measured in terms of consumers progressing from one stage to the next. However, the order of stages in the model, as well as whether consumers go through all steps, has been much debated. For example, a purchase can occur without interest or desire, perhaps when a low-involvement product is bought on impulse. Regardless of the order of the stages or consumers' progression through these stages, the AIDA concept helps marketers by suggesting which promotional strategy—that is, which plan for using the promotional mix—will be most effective.[19]

REVIEW LEARNING OUTCOME

LO5 Discuss the AIDA concept and its relationship to the promotional mix

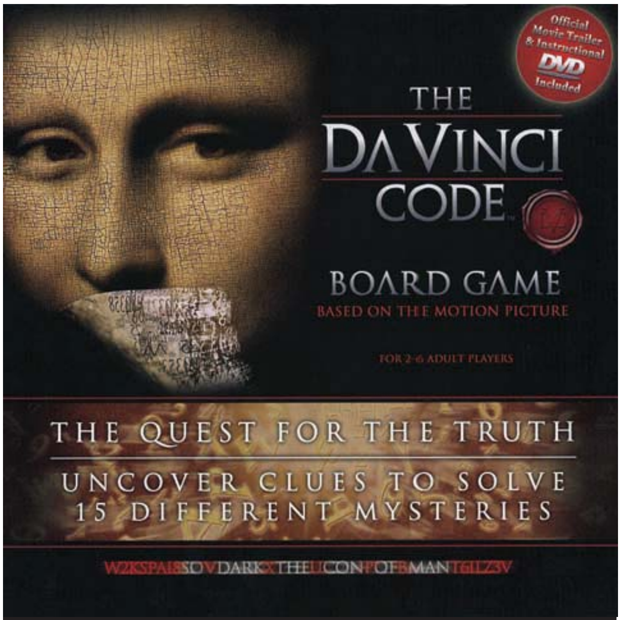
	Attention	Interest	Desire	Action
Advertising	✓+	✓+	✓	✓–
Public Relations	✓+	✓+	✓+	✓–
Sales Promotion	✓	✓	✓+	✓
Personal Selling	✓	✓+	✓+	✓+

LO6

Integrated Marketing Communications

Ideally, marketing communications from each promotional mix element (personal selling, advertising, sales promotion, and public relations) should be integrated—the message reaching the consumer should be the same regardless of whether it is from an advertisement, a salesperson in the field, a magazine article, or a coupon in a newspaper insert.

From the consumer's standpoint, a company's communications are already integrated. Consumers do not think in terms of the four elements of promotion: advertising, sales promotion, public relations, and personal selling. Instead, everything is an ad. In general, the only people who recognize the distinctions among these elements are the marketers themselves. Unfortunately, many marketers neglect this fact when planning promotional messages and fail to integrate their communication efforts from one element to the next. The most common rift typically occurs between personal selling and the other elements of the promotional mix.



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Moviemakers frequently use integrated marketing techniques to promote their films. Internet contests on Google, guide books from key cities in the story, and controversy over the movie's religious themes all contributed to the box-office success of *The Da Vinci Code*.

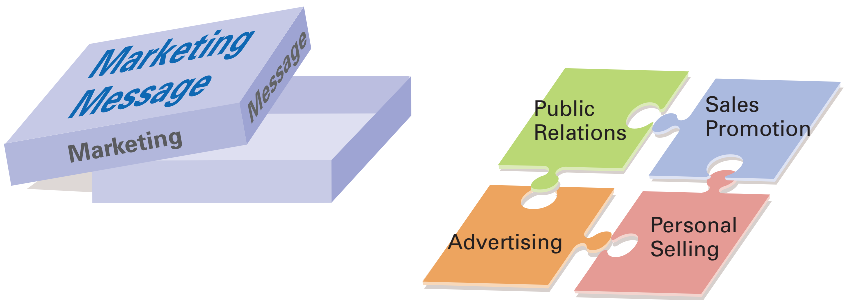
This unintegrated, disjointed approach to promotion has propelled many companies to adopt the concept of **integrated marketing communications (IMC)**. IMC is the careful coordination of all promotional messages—traditional advertising, direct marketing, interactive, public relations, sales promotion, personal selling, event marketing, and other communications—for a product or service to assure the consistency of messages at every contact point where a company meets the consumer. Following the concept of IMC, marketing managers carefully work out the roles that various promotional elements will play in the marketing mix. Timing of promotional activities is coordinated, and the results of each campaign are carefully monitored to improve future use of the promotional mix tools. Typically, a marketing communications director is appointed who has overall responsibility for integrating the company's marketing communications.

Movie marketing campaigns benefit greatly from an IMC approach. Those campaigns that are most integrated generally have more impact and make a deeper impression on potential moviegoers, leading to higher box-office sales. An integrated marketing approach was used to introduce *The Da Vinci Code*. Excitement about the release of the film gathered momentum months in advance as the trailer was shown on the Internet and television. Along with the release of the trailer, the movie was supported by numerous merchandising efforts. Bookstores and gift shops stocked hardback, paperback, and special illustrated editions, as well as *Da Vinci Code* walking tours of key cities in the story, playing cards, calligraphy sets, music CDs, video games, podcasts and more. Google and Sony launched a game called "The Sony Ericsson Da Vinci Code Trail" in 22 languages. Players competed against each other online and then in a real life challenge in Paris. The winner was awarded a two week trip to Rome, Paris, London, and New York. The game did more than promote the movie, however. "Da Vinci Code Trail" familiarized people with Google's services beyond search and drove traffic to Sony's Web site, which rose 30 percent as a result of the promotion. Finally, before the movie's release, there were over 500,000 English language posts on blogs like Technorati, Google, IceRocket, and BlogPulse. The integrated marketing campaign (plus the religious controversy surrounding the story) helped the film generate over $77 million at the box office on opening weekend.[20]

The IMC concept has been growing in popularity for several reasons. First, the proliferation of thousands of media choices beyond traditional television has made promotion a more complicated task. Instead of promoting a product just through mass-media options, like television and magazines, promotional messages today can appear in many varied sources. Furthermore, the mass market has also fragmented—more selectively segmented markets and an increase in niche marketing have replaced the traditional broad market groups that marketers

REVIEW LEARNING OUTCOME

LO 6 Discuss the concept of integrated marketing communications



promoted to in years past. For instance, many popular magazines now have Spanish-language editions targeted toward America's growing Hispanic population. Finally, marketers have slashed their advertising spending in favor of promotional techniques that generate immediate sales responses and those whose effects are more easily measured, such as direct marketing. Thus, the interest in IMC is largely a reaction to the scrutiny that marketing communications has come under and, particularly, to suggestions that uncoordinated promotional activity leads to a strategy that is wasteful and inefficient.

LO7

Factors Affecting the Promotional Mix

Promotional mixes vary a great deal from one product and one industry to the next. Normally, advertising and personal selling are used to promote goods and services, and are supported and supplemented by sales promotion. Public relations helps develop a positive image for the organization and the product line. However, a firm may choose not to use all four promotional elements in its promotional mix, or it may choose to use them in varying degrees. The particular promotional mix chosen by a firm for a product or service depends on several factors: the nature of the product, the stage in the product life cycle, target market characteristics, the type of buying decision, funds available for promotion, and whether a push or a pull strategy will be used.

NATURE OF THE PRODUCT

Characteristics of the product itself can influence the promotional mix. For instance, a product can be classified as either a business product or a consumer product (refer to Chapters 7 and 10). As business products are often custom-tailored to the buyer's exact specifications, they are often not well suited to mass promotion. Therefore, producers of most business goods, such as computer systems or industrial machinery, rely more heavily on personal selling than on advertising. Informative personal selling is common for industrial installations, accessories, and component parts and materials. Advertising, however, still serves a purpose in promoting business goods. Advertisements in trade media may be used to create general buyer awareness and interest. Moreover, advertising can help locate potential customers for the sales force. For example, print media advertising often includes coupons soliciting the potential customer to "fill this out for more detailed information."

In contrast, because consumer products generally are not custom-made, they do not require the selling efforts of a company representative who can tailor them to the user's needs. Thus, consumer goods are promoted mainly through advertising to create brand familiarity. Television and radio advertising, consumer-oriented magazines, and increasingly the Internet and other highly targeted media are used extensively to promote consumer goods, especially nondurables. Sales promotion, the brand name, and the product's packaging are about twice as important for consumer goods as for business products. Persuasive personal selling is important at the retail level for shopping goods such as automobiles and appliances.

The costs and risks associated with a product also influence the promotional mix. As a general rule, when the costs or risks of using a product increase, personal selling becomes more important. Items that are a small part of a firm's budget (supply items) or of a consumer's budget (convenience products) do not require a salesperson to close the sale. In fact, inexpensive items cannot support the cost of a salesperson's time and effort unless the potential volume is high. On the other hand, expensive and complex machinery, new buildings, cars, and new homes represent a considerable investment. A salesperson must assure buyers that they are spending their money wisely and not taking an undue financial risk.

Social risk is an issue as well. Many consumer goods are not products of great social importance because they do not reflect social position. People do not experience much social risk in buying a loaf of bread or a candy bar. However, buying some shopping products and many specialty products such as jewelry and clothing does involve a social risk. Many consumers depend on sales personnel for guidance and advice in making the "proper" choice.

STAGE IN THE PRODUCT LIFE CYCLE

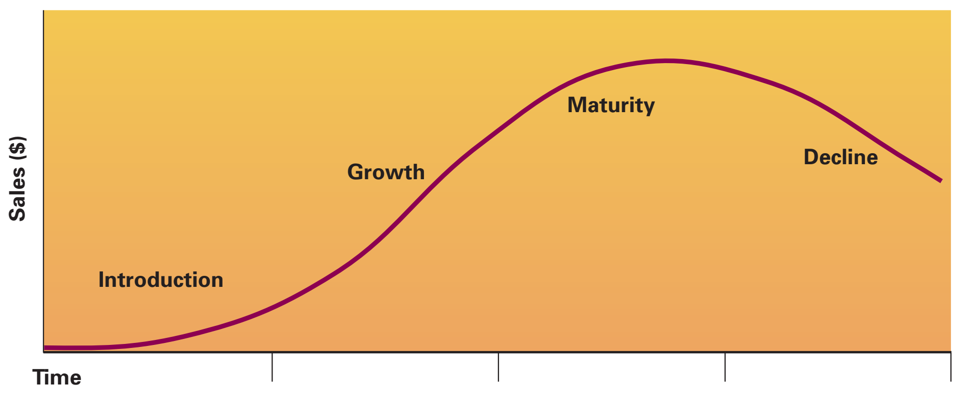
The product's stage in its life cycle is a big factor in designing a promotional mix (see Exhibit 16.4). During the *introduction stage,* the basic goal of promotion is to inform the target audience that the product is available. Initially, the emphasis is on the general product class—for example, mobile phones. The emphasis gradually changes to gaining attention for a particular brand, such as Nokia, Samsung, Sony Ericsson, or Motorola. Typically, both extensive advertising and public relations inform the target audience of the product class or brand and heighten awareness levels. Sales promotion encourages early trial of the product, and personal selling gets retailers to carry the product.

When the product reaches the *growth stage* of the life cycle, the promotion blend may shift. Often a change is necessary because different types of potential buyers are targeted. Although advertising and public relations continue to be major elements of the promotional mix, sales promotion can be reduced because consumers need fewer incentives to purchase. The promotional strategy is to emphasize the product's differential advantage over the competition. Persuasive promotion is used to build and maintain brand loyalty to support the product during the growth stage. By this stage, personal selling has usually succeeded in getting adequate distribution for the product.

As the product reaches the *maturity stage* of its life cycle, competition becomes more fierce, and thus persuasive and reminder advertising are more strongly

Exhibit 16.4

Product Life Cycle and the Promotional Mix



Preintroduction publicity; small amounts of advertising near introduction	Heavy advertising and public relations to build awareness; sales promotion to induce trial; personal selling to obtain distribution	Heavy advertising and public relations to build brand loyalty; decreasing use of sales promotion; personal selling to maintain distribution	Advertising slightly decreased — more persuasive and reminder in nature; increased use of sales promotion to build market share; personal selling to maintain distribution	Advertising and public relations drastically decreased; sales promotion and personal selling maintained at low levels

emphasized. Sales promotion comes back into focus as product sellers try to increase their market share.

All promotion, especially advertising, is reduced as the product enters the *decline stage*. Nevertheless, personal selling and sales promotion efforts may be maintained, particularly at the retail level.

TARGET MARKET CHARACTERISTICS

A target market characterized by widely scattered potential customers, highly informed buyers, and brand-loyal repeat purchasers generally requires a promotional mix with more advertising and sales promotion and less personal selling. Sometimes, however, personal selling is required even when buyers are well informed and geographically dispersed. Although industrial installations and component parts may be sold to extremely competent people with extensive education and work experience, salespeople must still be present to explain the product and work out the details of the purchase agreement.

Often firms sell goods and services in markets where potential customers are hard to locate. Print advertising can be used to find them. The reader is invited to call for more information or to mail in a reply card for a detailed brochure. As the calls or cards are received, salespeople are sent to visit the potential customers.

TYPE OF BUYING DECISION

The promotional mix also depends on the type of buying decision (routine or complex). For example, the most effective promotion for routine consumer decisions, like buying toothpaste or soft drinks, calls attention to the brand or reminds the consumer about the brand. Advertising and, especially, sales promotion are the most productive promotion tools to use for routine decisions.

If the decision is neither routine nor complex, advertising and public relations help establish awareness for the good or service. Suppose a man is looking for a bottle of wine to serve to his dinner guests. As a beer drinker, he is not familiar with wines, yet he has seen advertising for Robert Mondavi wine and has also read an article in a popular magazine about the Robert Mondavi winery. He may be more likely to buy this brand because he is already aware of it.

In contrast, consumers making complex buying decisions are more extensively involved. They rely on large amounts of information to help them reach a purchase decision. Personal selling is most effective in helping these consumers decide. For example, consumers thinking about buying a car usually depend on a salesperson to provide the information they need to reach a decision. Print advertising may also be used for high-involvement purchase decisions because it can often provide a large amount of information to the consumer.

AVAILABLE FUNDS

Money, or the lack of it, may easily be the most important factor in determining the promotional mix. A small, undercapitalized manufacturer may rely heavily on free publicity if its product is unique. If the situation warrants a sales force, a financially strained firm may turn to manufacturers' agents, who work on a commission basis with no advances or expense accounts. Even well-capitalized organizations may not be able to afford the advertising rates of publications like *Better Homes and Gardens, Reader's Digest,* and *The Wall Street Journal,* or the cost of running television commercials on *CSI* or the Super Bowl. The price of a high-profile advertisement in these media could support several salespeople for an entire year.

When funds are available to permit a mix of promotional elements, a firm will generally try to optimize its return on promotion dollars while minimizing the *cost per contact,* or the cost of reaching one member of the target market. In general, the cost per contact is very high for personal selling, public relations, and sales promotions like sampling and demonstrations. On the other hand, given the number of people national advertising reaches, it has a very low cost per contact.

Usually, there is a trade-off among the funds available, the number of people in the target market, the quality of communication needed, and the relative costs of the promotional elements. A company may have to forgo a full-page, color advertisement in *People* magazine in order to pay for a personal selling effort. Although the magazine ad will reach more people than personal selling, the high cost of the magazine space is a problem.

PUSH AND PULL STRATEGIES

push strategy
A marketing strategy that uses aggressive personal selling and trade advertising to convince a wholesaler or a retailer to carry and sell particular merchandise.

pull strategy
A marketing strategy that stimulates consumer demand to obtain product distribution.

The last factor that affects the promotional mix is whether to use a push or a pull promotional strategy. Manufacturers may use aggressive personal selling and trade advertising to convince a wholesaler or a retailer to carry and sell their merchandise. This approach is known as a **push strategy** (see Exhibit 16.5). The wholesaler, in turn, must often push the merchandise forward by persuading the retailer to handle the goods. The retailer then uses advertising, displays, and other forms of promotion to convince the consumer to buy the "pushed" products. This concept also applies to services. For example, the Jamaican Tourism Board targets promotions to travel agencies, which, in turn, tell their customers about the benefits of vacationing in Jamaica.

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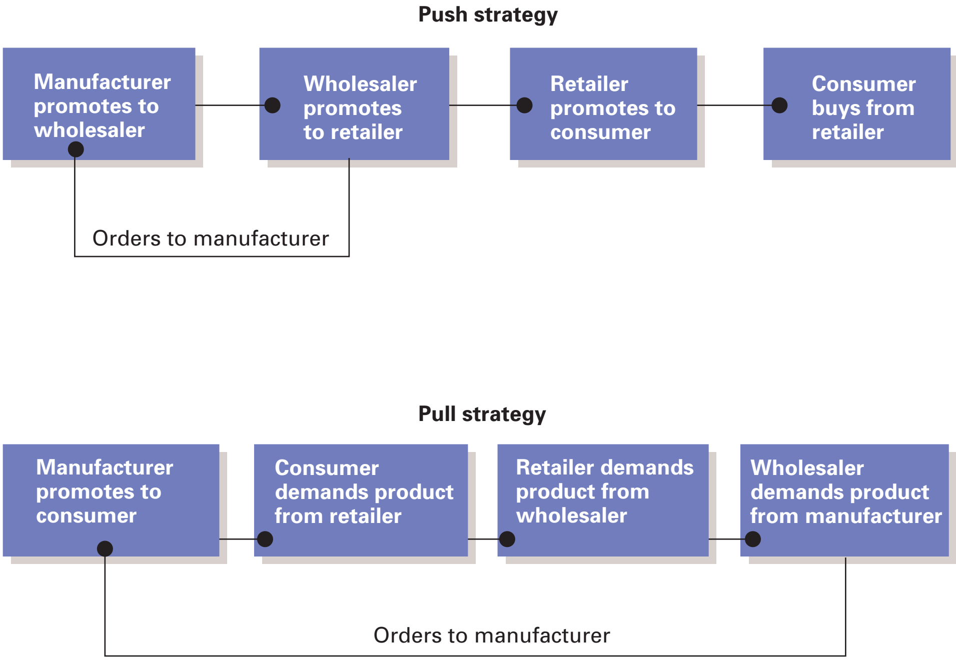
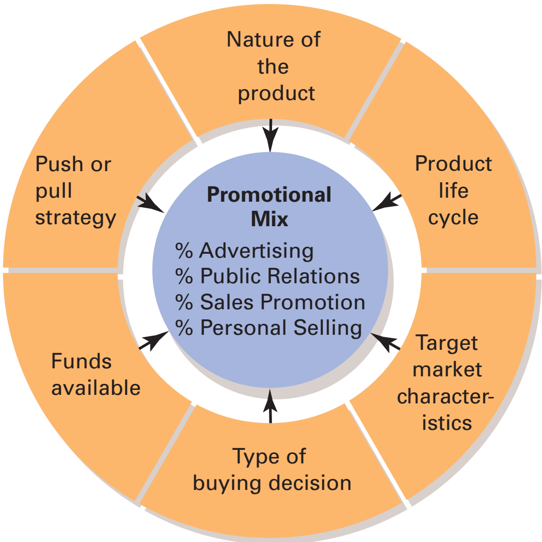
At the other extreme is a **pull strategy,** which stimulates consumer demand to obtain product distribution. Rather than trying to sell to the wholesaler, the manufacturer using a pull strategy focuses its promotional efforts on end consumers or opinion leaders. For example, Procter & Gamble recently spent $100 million on an advertising campaign to promote its new toothpaste. P & G's new Crest Pro-Health claims to deliver everything a consumer could want in one tube—it supposedly protects against gingivitis, plaque, cavities, sensitivity, stains, and it freshens breath. The theme of the campaign, targeted to the information-seeking customer, is "Healthy, beautiful smiles for life."[21] Consumers responded positively to the campaign and began demanding the product from their retailer. The retailer ordered the merchandise from the wholesaler. The wholesaler, confronted with rising demand, then placed an order for the "pulled" merchandise from the manufacturer. Consumer

Exhibit 16.5
Push Strategy versus Pull Strategy



REVIEW LEARNING OUTCOME

LO7 Describe the factors that affect the promotional mix



demand pulled the product through the channel of distribution (see Exhibit 16.5). Heavy sampling, introductory consumer advertising, cents-off campaigns, and couponing are part of a pull strategy. Procter & Gamble flooded dental offices with product samples and informational materials in hopes of generating favorable testimonials from users. Similarly, Splenda No Calorie Sweetener offered free samples, recipes, and a coupon to potential consumers who tried the product.[22]

Rarely does a company use a pull or a push strategy exclusively. Instead, the mix will emphasize one of these strategies. For example, pharmaceutical companies generally use a push strategy, through personal selling and trade advertising, to promote their drugs and therapies to physicians. Sales presentations and advertisements in medical journals give physicians the detailed information they need to prescribe medication to their patients. Most pharmaceutical companies supplement their push promotional strategy with a pull strategy targeted directly to potential patients through advertisements in consumer magazines and on television.

3,500 < people interviewed by Sara Lee Corp. before it innovated Kiwi shoe polish

media contacts generated by Absolut's Porsche taxis in Germany > **15 million**

112.8 million < blogs tracked by Technorati

percentage of blogs updated weekly > **10**

70 < percentage of e-mail messages that are spam

iPods sold per minute during the 2005 Christmas season > **100**

$100 million < cost of Procter & Gamble's recent advertising campaign for Crest Pro-Health

22 < languages in which Google and Sony offered "The Sony Ericsson Da Vinci Code Trail"

percentage of increased traffic at Sony's Web site during the promotion > **30**

$77 billion < ticket sales for *The DaVinci Code's* opening weekend

Review and Applications

LO1 **Discuss the role of promotion in the marketing mix.** Promotion is communication by marketers that informs, persuades, and reminds potential buyers of a product in order to influence an opinion or elicit a response. Promotional strategy is the plan for using the elements of promotion—advertising, public relations, sales promotion, and personal selling—to meet the firm's overall objectives and marketing goals. Based on these objectives, the elements of the promotional strategy become a coordinated promotion plan. The promotion plan then becomes an integral part of the total marketing strategy for reaching the target market along with product, distribution, and price.

1.1 What is a promotional strategy? Explain the concept of a competitive advantage in relation to promotional strategy.

LO2 **Describe the communication process.** The communication process has several steps. When an individual or organization has a message it wishes to convey to a target audience, it encodes that message using language and symbols familiar to the intended receiver and sends the message through a channel of communication. Noise in the transmission channel distorts the source's intended message. Reception occurs if the message falls within the receiver's frame of reference. The receiver decodes the message and usually provides feedback to the source. Normally, feedback is direct for interpersonal communication and indirect for mass communication.

2.1 Why is understanding the target market a crucial aspect of the communication process?

LO3

Explain the goals of promotion. The fundamental goals of promotion are to induce, modify, or reinforce behavior by informing, persuading, and reminding. Informative promotion explains a good's or service's purpose and benefits. Promotion that informs the consumer is typically used to increase demand for a general product category or to introduce a new good or service. Persuasive promotion is designed to stimulate a purchase or an action. Promotion that persuades the consumer to buy is essential during the growth stage of the product life cycle, when competition becomes fierce. Reminder promotion is used to keep the product and brand name in the public's mind. Promotions that remind are generally used during the maturity stage of the product life cycle.

3.1 Why might a marketing manager choose to promote his or her product using persuasion? Give some current examples of persuasive promotion.

3.2 Choose a partner from class and go together to interview the owners or managers of several small businesses in your city. Ask them what their promotional objectives are and why. Are they trying to inform, persuade, or remind customers to do business with them? Also determine whether they believe they have an awareness problem or whether they need to persuade customers to come to them instead of to competitors. Ask them to list the characteristics of their primary market, the strengths and weaknesses of their direct competitors, and how they are positioning their store to compete. Prepare a report to present in class summarizing your findings.

LO4

Discuss the elements of the promotional mix. The elements of the promotional mix include advertising, public relations, sales promotion, and personal selling. Advertising is a form of impersonal, one-way mass communication paid for by the source. Public relations is the function of promotion concerned with a firm's public image. Sales promotion is typically used to back up other components of the promotional mix by stimulating immediate demand. Finally, personal selling typically involves direct communication, in person or by telephone; the seller tries to initiate a purchase by informing and persuading one or more potential buyers.

4.1 As the promotional manager for a new line of cosmetics targeted to preteen girls, you have been assigned the task of deciding which promotional mix elements—advertising, public relations, sales promotion, and personal selling—should be used in promoting it. Your budget for promoting the preteen cosmetics line is limited. Write a promotional plan explaining your choice of promotional mix elements given the nature of the product, the stage in the product life cycle, the target market characteristics, the type of buying decision, available funds, and the use of a pull or push strategy.

LO5

Discuss the AIDA concept and its relationship to the promotional mix. The AIDA model outlines the four basic stages in the purchase decision-making process, which are initiated and propelled by promotional activities: (1) attention, (2) interest, (3) desire, and (4) action. The components of the promotional mix have varying levels of influence at each stage of the AIDA model. Advertising is a good tool for increasing awareness and knowledge of a good or service. Sales promotion is effective when consumers are at the purchase stage of the decision-making process. Personal selling is most effective in developing customer interest and desire.

5.1 Discuss the AIDA concept. How do these different stages of consumer involvement affect the promotional mix?

5.2 How does a Web site's ease of use affect its ability to create attention, interest, desire, and action? Visit the kitchen and bath pages of Kohler's Web site (**http:// www.kohler.com**) and determine how successful the company is at moving consumers through the AIDA process.

LO6

Discuss the concept of integrated marketing communications. Integrated marketing communications is the careful coordination of all promotional messages for a product or service to assure the consistency of messages at every contact point where a company meets the consumer—advertising, sales promotion, personal selling, public relations, as well as direct marketing, packaging, and other forms of communication. Marketing managers carefully coordinate all promotional activities to ensure that consumers see and hear one message. Integrated marketing communications has received more attention in recent years due to the proliferation of media choices, the fragmentation of mass markets into more segmented niches, and the decrease in advertising spending in favor of promotional techniques that generate an immediate sales response.

6.1 Discuss the importance of integrated marketing communications. Give some current examples of companies that are and are not practicing IMC.

ONLINE

6.2 What do you think is the role of Hallmark's Web site (**http://www.hallmark.com**) in the company's integrated marketing communications plan? What seems to be the marketing function of the site? Do you think the site is effective?

LO7

Describe the factors that affect the promotional mix. Promotion managers consider many factors when creating promotional mixes. These factors include the nature of the product, product life-cycle stage, target market characteristics, the type of buying decision involved, availability of funds, and feasibility of push or pull strategies. Because most business products tend to be custom-tailored to the buyer's exact specifications, the marketing manager may choose a promotional mix that relies more heavily on personal selling. On the other hand, consumer products are generally mass produced and lend themselves more to mass promotional efforts such as advertising and sales promotion. As products move through different stages of the product life cycle, marketers will choose to use different promotional elements. For example, advertising is emphasized more in the introductory stage of the product life cycle than in the decline stage. Characteristics of the target market, such as geographic location of potential buyers and brand loyalty, influence the promotional mix as does whether the buying decision is complex or routine. The amount of funds a firm has to allocate to promotion may also help determine the promotional mix. Small firms with limited funds may rely more heavily on public relations, whereas larger firms may be able to afford broadcast or print advertising. Last, if a firm uses a push strategy to promote the product or service, the marketing manager may choose to use aggressive advertising and personal selling to wholesalers and retailers. If a pull strategy is chosen, then the manager often relies on aggressive mass promotion, such as advertising and sales promotion, to stimulate consumer demand.

7.1 Explain the difference between a "pull" and a "push" promotional strategy. Under what conditions should each strategy be used?

ONLINE

7.2 Use Radioguide.com (**http://www.radioguide.com**) to find a listing of radio Web sites in your area. View several of the stations' sites and compare the promotions featured. What conclusions can you draw about the target market of each station based on the types of promotions they are currently running? Would any of the promotions entice you to tune to a station that you normally don't listen to?

ONLINE

7.3 Visit **http://www.teenresearch.com**. What research can this company offer about the size and growth of the teen market, the buying power of teenagers, and their buying habits? Why might these statistics be important to a company targeting teenagers in terms of marketing communications and promotion strategy?

Key Terms

AIDA concept	486	feedback	480	promotion	476
channel	479	integrated marketing communications (IMC)	488	promotional mix	483
communication	477	interpersonal communication	477	promotional strategy	476
competitive advantage	476	mass communication	477	pull strategy	493
corporate blogs	481	noise	479	push strategy	493
decoding	479	noncorporate blogs	481	receiver	479
encoding	479			sender	478

Exercises

APPLICATION EXERCISE 1

Many people are not aware of the rationale behind certain advertising messages. "Why do Infiniti ads show rocks and trees instead of automobiles?" "If car safety is so important, why do automobile ads often show cars skidding on wet, shiny surfaces?" "Target's ads are funky, with all the bright colors and product packaging, but what's the message?"

One way to understand the vagaries of the encoding process is to think of the popular board game *Taboo* by Hasbro. In this game, each team tries to get its members to guess a word without using obvious word clues. For example, to get the team to guess "apple," you may not say such words as *red, fruit, pie, cider,* or *core.* Sometimes advertising is like *Taboo* in that advertisers are not allowed to use certain words or descriptions. For example, pharmaceutical companies are not permitted to make certain claims or to say what a drug treats unless the ad also mentions the potential side effects. Language choices are also limited in advertising. To appreciate this, you can apply the *Taboo* game rules in an advertising format.[23]

Activities

1. Select a product from the list below, and then create a print advertisement or a television storyboard for that product. As part of the exercise, give your product a brand name. Taboo words, visuals, and concepts are given for each product type. Taboo items cannot be present in your work.

Product	**Taboo Words, Visuals, and Concepts**
Deodorant	Odor, underarm, perspiration, smell, sweat
Pain reliever	Pain, aches, fever, child-proof cap, gel
Soft drinks	Sugar-free, refreshing, thirst, swimwear, any celebrity

2. Now create a second ad or storyboard for your product. This time, however, you must use all the words, visuals, and concepts that are listed in the right column.

Product	**Must-Use Words, Visuals, and Concepts**
Deodorant	A romantic couple, monster trucks
Pain reliever	A mother and child, oatmeal, homework
Soft drinks	A cup of coffee, cookies, birthday cake, wine

APPLICATION EXERCISE 2

An important concept in promotion is semiotics, or the study of meaning and meaning-producing events. An understanding of semiotics can help you not only to identify objects (denotation) but also to grasp the utility of images and associations (connotation). By manipulating connotations of objects in advertising, you can create, change, or reinforce images for products. Thus, semiotics is a powerful tool for brand management and promotion.[24]

Activities

1. Make a list of ten images and associations that come to mind for each of the following items: baseball, vinyl record album, spoon, rubber band.
2. Look through magazines and see if you can find print advertisements that include each of the items (baseball, vinyl record album, spoon, rubber band) in a supporting role. What seems to be the message of each ad? How does the item help create or reinforce an image for the product being sold in the ad?
3. Think of an everyday object of your own. What are its likely connotations? For example, a dog in a car might signal a family vehicle, but a dog also connotes loyalty, "man's best friend," and dependability. What images and associations are likely with your item? Make a list of as many as you can.
4. Now use your object and list of associations to create an image for another product. Think of the likely connotations your object will have for a certain target market and how such connotations can support a brand image. For example, if your everyday object is a candle, you might choose lingerie for your product, based on a candle's romantic connotations.

ETHICS EXERCISE

Integrated Marketing Solutions is a consumer-products marketing services firm. Currently, the firm is handling the launch of a new book for one of its publishing clients. The campaign includes advance review copies for key book reviewers, "Coming Soon" posters for booksellers, an author book-signing tour, and several television interviews. Everything has been produced and scheduled for release next week. Today, Jane Kershaw, the account executive, has learned that although the book received numerous favorable reviews, the review quoted on all of the promotional materials is fabricated.

Questions

1. What should Jane do? Why?
2. What does the AMA Statement of Ethics say about accuracy in promotional materials? Go to **http://www.marketingpower.com** and review the code. Then, write a brief paragraph describing how the AMA Statement of Ethics relates to this issue.

Case Study: Wicked

© AP PHOTO/KATHY WILLENS

WICKED AWESOME! MUSICAL ENCHANTS RECORD CROWDS AFTER ROCKY START

When the curtains first lifted on the Broadway musical *Wicked,* it appeared that audiences had been scared away from the box office. The Gershwin Theater was rarely full, and a production that had cost over $14 million posted advance ticket sales of only $9 million. Crippled by cost overruns, cast changes, song rewrites, and a 2003 start date that was much later than projected, excitement and enthusiasm waned for what was once a much-anticipated show.

Based on Gregory Maguire's best-selling 1995 novel of the same name, the story is a prequel to Frank Baum's 1939 classic, *The Wizard of Oz.* The musical examines the lives of two teenage witches, Glinda and Elphaba, and wonders which one is truly evil. Glinda, a beautiful, ambitious, and popular blond, grows up to become the Good Witch; Elphaba, a green-skinned, intelligent, free-spirited rebel, develops into the nefarious Wicked Witch of the West. Elaborate sets, lighting, and costumes and a score by Academy Award–winning songwriter Stephen Schwartz did not impress the *New York Times*, however. Its scathing review claimed, "There's trouble in Emerald City . . . [it's] a sermon of a musical."

Unfazed, *Wicked* producer Marc Platt, a former Universal Pictures executive, never lost faith in his production. He remained convinced that if he could just get people in the door, they would leave completely captivated by what he considered a truly exceptional experience. So he cut ticket prices by 30 percent and watched as patrons began to make repeat ticket purchases during intermission. After the shows, swarms of enthralled teenage girls began to gather outside the stage door in hopes of meeting the cast.

As the target market emerged before his eyes, Platt leveraged his Hollywood experience to turn *Wicked* into a musical marketing machine. The hot ticket sales during show intermissions indicated that the show's success would hinge on word-of-mouth referrals from the show's core audience—teenage girls. To get more of them talking, Platt and the marketing team published feature articles on the show's Web site and seeded Internet chat rooms with *Wicked*-related topics. An all-out promotions blitz ensued.

Wicked lined up character endorsement deals with makeup manufacturer, Stila, and sent hot new stars Kristin Chenoweth and Idina Menzel to Sephora stores to give makeovers to teen fans with Glinda facial glitter and Elphaba lipstick. In an interesting twist on *American Idol, Wicked* karaoke contests at malls served as fake auditions that awarded real tickets to the most passionate fans. Radio promos in New York and Chicago were supported by advertising at Macy's and in *Elle Girl* magazine for a Halloween campaign that lasted a month.

As the show became profitable, two U.S. tours were launched. The shows routinely sell out, and yearly revenues are now close to $200 million. Tickets to the show on Broadway now command a record-tying $110, and the show's take is about $1.3 million a week in New York alone. Mike Isaacson, vice president of the Fox Theatre in St. Louis, sold an amazing $1.5 million worth of tickets a mere 48 hours after they went on sale. "This show is a rocket because it's attracting people from teenagers to grandparents," he mused.

Day-of-show raffles for tickets at sold-out venues give a few lucky patrons a chance to buy $25 tickets. Those raffles generally appeal to younger theatergoers, but those witch-wannabes bring mom and dad out for the night of mischief too. And their dollars help fund purchases of merchandise at the traveling OzDust Boutiques. Items like *Wicked*-branded golf balls, T-shirts, necklaces, and CDs of the show's musical numbers sell at the stands and at **http://www.wickedthemusical.com**. Sales generate weekly merchandise receipts of more than $300,000. But that doesn't surprise Marc Platt. Reflecting on the show's universal premise, he quips, "There's a little green girl inside all of us."[25]

Questions

1. Identify and describe the elements of *Wicked's* promotional mix.
2. Describe how the AIDA process worked for various *Wicked* promotions. Which one do you think was most effective?
3. Did *Wicked* use a push or a pull promotional strategy? Explain.
4. As *Wicked* progresses through its life cycle, what changes would you recommend making to the current promotional mix? Why?

Company Clips

VANS—OFF THE WALL AND ON TARGET

You have undoubtedly heard of Vans. The company has sold footwear, apparel, and extreme sports equipment for over 40 years using the distinct tagline, "Off the Wall." The company's founder wanted to control his own retail channel, so he transformed his manufacturing company into a marketing company. Always carefully protecting its unique brand image, Vans has crafted successful marketing messages and promotions that resonate with the youth culture that represents the company's target market. This video examines the carefully planned strategy that Vans developed to create loyalty in a fickle niche market.

Questions

1. Does Vans use a push or pull strategy to market its apparel? How does Steve feel about the two strategies?
2. What does Steve mean when he refers to tours and events as "planting seeds?"
3. Describe Vans' pyramid strategy. How does it protect the brand?
4. How does Steve's hands-on approach to events and promotion benefit the company?

Marketing & You Results

Higher scores on this scale indicate that others perceive you to be responsive, warm, and a good listener. A high score also corresponds to a willingness to mentor others. If your score is low, it indicates that you don't actively encourage other people to share information about themselves with you. That doesn't mean you are a poor listener, however. Rather, you prefer not to take the initiative in the interaction.

ANATOMY OF AN Integrated Marketing Campaign

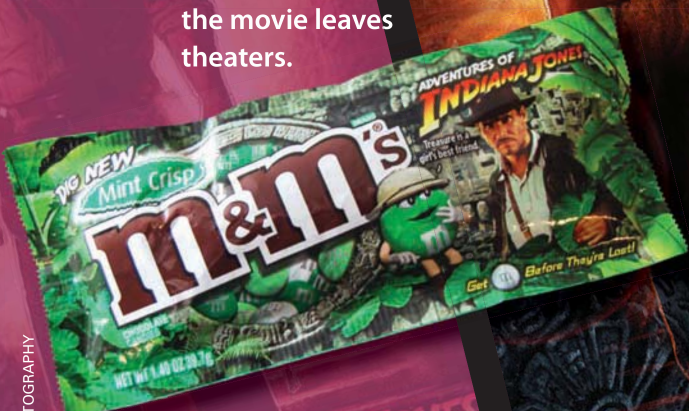
Indiana Jones movie

Lucas Film Ltd. used integrated marketing communications to ensure that *Indiana Jones and the Kingdom of the Crystal Skull* was widely and consistently promoted before its release.

NASCAR cars increase publicity.

Hallmark greeting cards and Scholastic books hold kids' interest even after the movie leaves theaters.

Legos and Kelloggs' cereal attracts kids.



Burger King's "Indy Double Whopper" and Mars' M&Ms tie the movie to summer fun.

PHOTOS COURTESY OF CHAPEL HOUSE PHOTOGRAPHY

Advertising and Public Relations

CHAPTER 17

Learning Outcomes

LO 1 Discuss the effects of advertising on market share and consumers

LO 2 Identify the major types of advertising

LO 3 Discuss the creative decisions in developing an advertising campaign

LO 4 Describe media evaluation and selection techniques

LO 5 Discuss the role of public relations in the promotional mix

PR NEWSFOTO/© PEPSICO

LO 1

The Effects of Advertising

advertising
Impersonal, one-way mass communication about a product or organization that is paid for by a marketer.

sales promotion
Marketing activities—other than personal selling, advertising, and public relations—that stimulate consumer buying and dealer effectiveness.

Advertising is defined as any form of impersonal, paid communication in which the sponsor or company is identified. It is a popular form of promotion, especially for consumer packaged goods and services. Advertising expenditures increase annually and were forecasted at nearly $480 billion worldwide in 2008. In 2005, 32 companies spent over $1 billion each; together, they accounted for about 22 percent of total ad spending. Among the top brands advertised by these companies were Verizon Communications, Olay, Crest, and Tylenol.[1]

Recent Bureau of Labor Statistics data show that advertising and marketing services—agencies and other firms that provide marketing and communications services to marketers—employ an estimated 800,000 people. About another 900,000 people work in media advertising, such as newspapers, broadcast and cable TV, radio, magazines and internet media companies.[2] However, there is a change-up underway in the outlook for advertising and marketing services workforce versus media advertising workforce. A dramatic rise in the use of marketing consultancy put advertising and marketing services employment at record highs in 2007, while record low newspaper employment has caused a major slump in total media employment.[3]

The amount of money budgeted for advertising by some firms is staggering (see Exhibit 17.1). Procter & Gamble, AT&T, General Motors, and Time Warner each spend almost $4 billion annually in the United States on national advertising alone. That's about $10 million a day on national advertising. If local advertising, sales promotion, and public relations are included, this figure rises much higher. Over 100 companies spend more than $300 million each on advertising every year. In 2007, those top 100 U.S. advertisers increased ad spending only by a modest 3.1 percent, yet they achieved record annual spending of $104.8 billion.[4]

Spending on advertising varies by industry. For example, the game and toy industry has one of the highest ratios of advertising dollars to sales. For every dollar of merchandise sold in the toy industry, about 12 to 15 cents is spent on advertising the toy to consumers. Book publishers spend roughly 27 cents on advertising for every dollar of book revenue. Other consumer goods manufacturers that spend heavily on advertising in relation to total sales include sugar and

Marketing & You

What do you think of television advertising?

Using the following scale, enter your answers on the lines provided.

1	2	3	4	5
Strongly disagree	Disagree	Neutral	Agree	Strongly agree

— TV advertising is a good way to learn what products and services are available.

— TV advertising results in better products for the public.

— In general, TV advertising presents a true picture of the product advertised.

— You can trust brands advertised on TV more than brands not advertised on TV.

— TV advertising helps raise our standard of living.

— TV advertisements help me find products that match my personality and interests.

— TV advertising helps me to know which brands have the features I am looking for.

— TV advertising gives me a good idea about products by showing the kinds of people who use them.

— TV advertising helps me buy the best brand for the price.

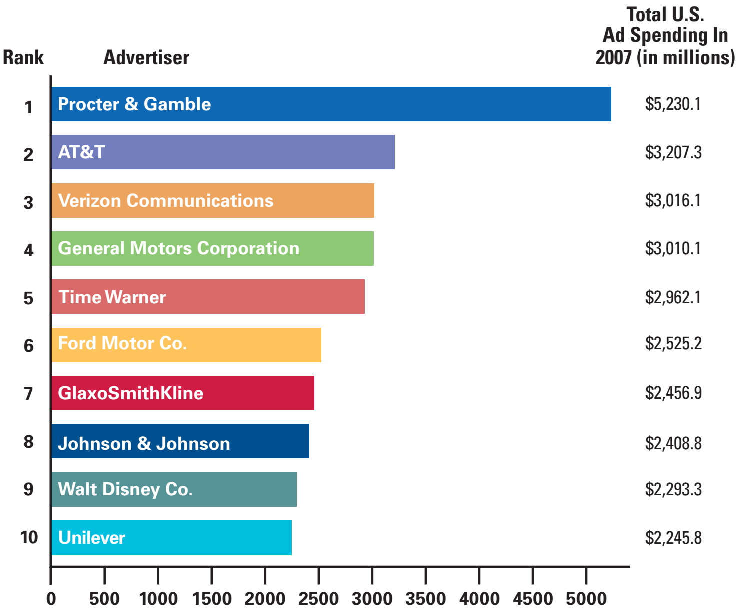
— I am willing to pay more for a product that is advertised on TV.

Total your score, and find out what it means at the end of the chapter.

confectionery products manufacturers, leather manufacturers, watchmakers, perfume and cosmetic manufacturers, detergent makers, and wine and liquor companies.[5]

Exhibit 17.1

Top Ten Leaders by U.S. Advertising Spending



Source: Advertising Age, June 23, 2008.

ADVERTISING AND MARKET SHARE

Today's most successful brands of consumer goods, like Ivory soap and Coca-Cola, were built by heavy advertising and marketing investments long ago. Today's advertising dollars are spent on maintaining brand awareness and market share.

New brands with a small market share tend to spend proportionately more for advertising and sales promotion than those with a large market share, typically for two reasons. First, beyond a certain level of spending for advertising and sales promotion, diminishing returns set in. That is, sales or market share begins to decrease no matter how much is spent on advertising and sales promotion. This phenomenon is called the **advertising response function.** Understanding the advertising response function helps marketers use budgets wisely. A market leader like Johnson & Johnson's Neutrogena typically spends proportionately less on advertising than a newcomer like Jergens' Natural Glow Daily Moisturizer brand. Jergens spends more on its brand to gain attention and increase market share. Neutrogena, on the other hand, spends only as much as is needed to maintain market share; anything more would produce diminishing benefits. Neutrogena has already captured the attention of the majority of its target market. It only needs to remind customers of its product.

advertising response function
A phenomenon in which spending for advertising and sales promotion increases sales or market share up to a certain level but then produces diminishing returns.

The second reason that new brands tend to require higher spending for advertising and sales promotion is that a certain minimum level of exposure is needed to measurably affect purchase habits. If Jergens advertised Natural Glow Daily Moisturizer in only one or two publications and bought only one or two television spots, it certainly would not achieve the exposure needed to penetrate consumers' perceptual defenses, gain attention, and ultimately affect purchase intentions. Instead, Natural Glow Daily Moisturizer was advertised in many different media for a sustained time.

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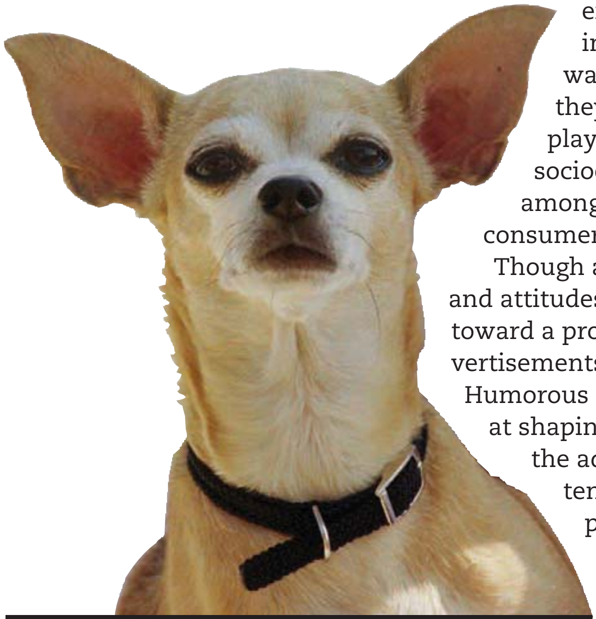
THE EFFECTS OF ADVERTISING ON CONSUMERS

Advertising affects consumers' daily lives, informing them about products and services and influencing their attitudes, beliefs, and ultimately their purchases. The average U.S. citizen is exposed to hundreds of advertisements a day from all types of advertising media. In the television medium alone, researchers estimate that the average viewer watches at least six hours of commercial television messages a week. In addition, that person is



The best results with humorous ads are achieved by making the message relevant to the product like the talking Chihuahua with a "south of the border" accent Taco Bell used in its advertising campaigns.

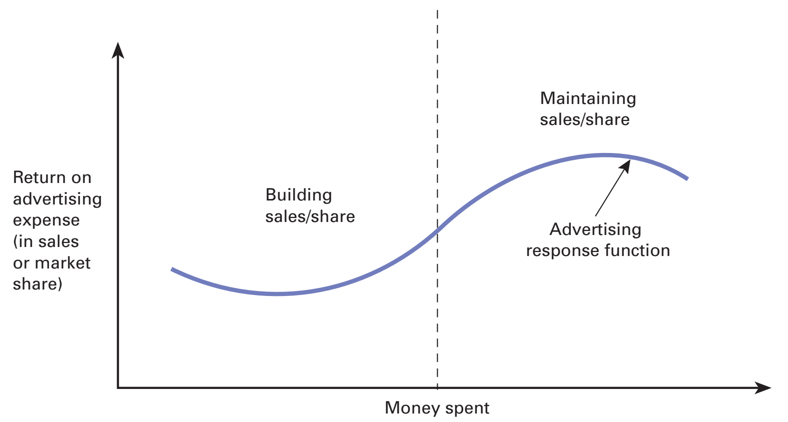
exposed to countless print ads and promotional messages seen in other places. Advertising affects the TV programs people watch, the content of the newspapers they read, the politicians they elect, the medicines they take, and the toys their children play with. Consequently, the influence of advertising on the U.S. socioeconomic system has been the subject of extensive debate among economists, marketers, sociologists, psychologists, politicians, consumerists, and many others.

Though advertising cannot change consumers' deeply rooted values and attitudes, it may succeed in transforming a person's negative attitude toward a product into a positive one. For instance, serious or dramatic advertisements are more effective at changing consumers' negative attitudes. Humorous ads, on the other hand, have been shown to be more effective at shaping attitudes when consumers already have a positive image of the advertised brand.[6] However, as much as humor in advertising tends to improve brand recognition, it does not necessarily improve product recall, message credibility, or buying intentions. Consumers who find the ad funny may have good feelings about the product, but their purchasing decisions will not be affected unless they can actually recall the brand. The best results with humorous ads are achieved by making the message relevant to the product. For example, Taco Bell saw a substantial rise in sales after promoting a tiny talking Chihuahua who was crazy about their product, constantly demanding to be fed by saying, "yo quiero Taco Bell." The phrase caught on and got people repeating—and remembering—the company's name across the country. The actual content of the commercial reinforced the company's message in a relevant manner.[7]

Advertising can also affect the way consumers rank a brand's attributes, such as color, taste, smell, and texture. For example, in years past, car ads emphasized such brand attributes as roominess, speed, and low maintenance. Today, however, car marketers have added safety, versatility, and customization to the list. Safety

REVIEW LEARNING OUTCOME

LO 1 Discuss the effects of advertising on market share and consumers



Advertising can:
- ✓ change negative attitude to positive
- ✓ reinforce positive attitude
- ✓ affect how consumers rank brand attributes

features like antilock brakes, power door locks, and front and side air bags are now a standard part of the message in many carmakers' ads. Toyota Scion appeals to consumers' sense of individuality by allowing purchasers to custom-design their cars by selecting features such as the steering wheel color, multi-shade illuminated cup holders, and "sport" pedals.[8]

LO 2

Major Types of Advertising

The firm's promotional objectives determine the type of advertising it uses. If the goal of the promotion plan is to build up the image of the company or the industry, institutional advertising may be used. In contrast, if the advertiser wants to enhance the sales of a specific good or service, product advertising is used.

INSTITUTIONAL ADVERTISING

COURTESY TIME WARNER, INC.

Historically, advertising in the United States has been product oriented. Today, however, companies market multiple products and need a different type of advertising. Institutional advertising, or corporate advertising, promotes the corporation as a whole and is designed to establish, change, or maintain the corporation's identity. It usually does not ask the audience to do anything but maintain a favorable attitude toward the advertiser and its goods and services. For example, when Time Warner dropped AOL from the company's corporate brand name, it hired a branding agency to develop institutional advertising to reposition the brand without the Internet unit and refocus the image on Time Warner as a media giant. In designing the "rebranding," executives did not want a radical change. Rather they wanted to "freshen" the previous image and maintain its favorable status. The logo itself changed in texture, color, and typeface. In addition to changing the logo on buildings, business cards, and stationery, the company changed its stock ticker symbol to reflect the new image.[9]

A form of institutional advertising called advocacy advertising is typically used to safeguard against negative consumer attitudes and to enhance the company's credibility among consumers who already favor its position. Often corporations use advocacy advertising to express their views on controversial issues. At other times, firms' advocacy campaigns react to criticism or blame, some in direct response to criticism by the media. Other advocacy campaigns may try to ward off increased regulation, damaging legislation, or an unfavorable outcome in a lawsuit. The tobacco companies have utilized "good citizen campaigns" in the United States and around the world in an effort to create a positive public image for themselves after losing several class-action suits and being accused of targeting children with their marketing campaigns. In an effort to improve its corporate image, Philip Morris has been spending more than $120 million a year promoting its environmental and community development programs, such as building homes for Habitat for Humanity, making donations to food banks, and supporting meal programs for seniors and shelters for battered women.[10]

PRODUCT ADVERTISING

Unlike institutional advertising, product advertising promotes the benefits of a specific good or service. The product's stage in its life cycle often determines which type of product advertising is used: pioneering advertising, competitive advertising, or comparative advertising.

Pioneering Advertising

Pioneering advertising is intended to stimulate primary demand for a new product or product category. Heavily used during the introductory stage of the product life cycle, pioneering advertising offers consumers in-depth information about the

institutional advertising
A form of advertising designed to enhance a company's image rather than promote a particular product.

product advertising
A form of advertising that touts the benefits of a specific good or service.

advocacy advertising
A form of advertising in which an organization expresses its views on controversial issues or responds to media attacks.

pioneering advertising
A form of advertising designed to stimulate primary demand for a new product or product category.

competitive advertising
A form of advertising designed to influence demand for a specific brand.

comparative advertising
A form of advertising that compares two or more specifically named or shown competing brands on one or more specific attributes.

benefits of the product class. Pioneering advertising also seeks to create interest. Pharmaceutical companies are the latest big players in pioneering advertising. For instance, one pharma giant, Pfizer, has steadily ramped up consumer advertising of a new drug, Lyrica—first approved in 2005 by the FDA to treat pain caused by diabetic nerve damage. Then Pfizer found a broader market for Lyrica when it was approved in 2007 for treatment of the disputed pain condition fibromyalgia. In just the first half of 2007, Pfizer spent $46 million on a new ad campaign for Lyrica as a treatment for fibromylagia, compared with $33 million in 2006, in spite of the protest by many doctors who do not acknowledge fibromyalgia as a real medical condition. As yet, there are no biological tests to diagnose fibromyalgia, and the condition has not been linked to any environmental or biological causes. However, worldwide sales of Lyrica reached $1.8 billion in 2007, up 50 percent from 2006. Analysts predict sales will rise an additional 30 percent in 2008, helped by consumer advertising and the interest from other drug companies who see the potential for a major new market in aggressively pursuing fibromyalgia treatments.[11]

Virgin Atlantic airline used comparative advertising in its recent "Love from Above" campaign, which challenged consumers' lowered expectations for the perks of air travel. Instead of competing with other airlines for the lowest fares, Virgin Atlantics' campaign focuses on its incomparable reputation for quality service.

PR NEWSFOTO/© VIRGIN ATLANTIC

Competitive Advertising

Firms use competitive or brand advertising when a product enters the growth phase of the product life cycle and other companies begin to enter the marketplace. Instead of building demand for the product category, the goal of competitive advertising is to influence demand for a specific brand. Often promotion becomes less informative and appeals more to emotions during this phase. Advertisements may begin to stress subtle differences between brands, with heavy emphasis on building recall of a brand name and creating a favorable attitude toward the brand. Automobile advertising has long used very competitive messages, drawing distinctions based on such factors as quality, performance, and image. Similarly, in an effort to obtain market share from competitors and to build brand awareness in the wireless industry, Nextel Communications signed a ten-year title sponsorship agreement with NASCAR. NASCAR executives, interested in building a younger fan base, consider the telecom industry one of the best ways to reach younger consumers because they always have a cell phone "stuck" to their ear.[12]

Comparative Advertising

Comparative advertising directly or indirectly compares two or more competing brands on one or more specific attributes. Some advertisers even use comparative advertising against their own brands. Products experiencing sluggish growth or those entering the marketplace against strong competitors are more likely to employ comparative claims in their advertising. For instance, Virgin Atlantic airline's "Love from Above" campaign deliberately challenges travelers' expectations of air travel as boring at best by asking questions such as "Shouldn't a seat recharge more than your laptop?" and "Shouldn't Flying Be Art?" Air travelers who are constantly exposed to price wars in the airline industry know full well how price cuts have affected service—or what's left of it—when it comes to air travel. Virgin Atlantic's campaign focuses on its unique reputation for treating its passengers as welcome guests, with premium seating throughout its planes, onboard bars, and complimentary limo service.[13]

Before the 1970s, comparative advertising was allowed only if the competing brand was veiled and unidentified. In 1971, however, the Federal Trade Commission (FTC) fostered the growth of comparative advertising by saying that it provided information to the customer and that advertisers were more skillful than the government in communicating this information. Federal rulings prohibit advertisers from falsely describing competitors' products and allow competitors to sue if ads show their products or mention their brand names in an incorrect or false manner.

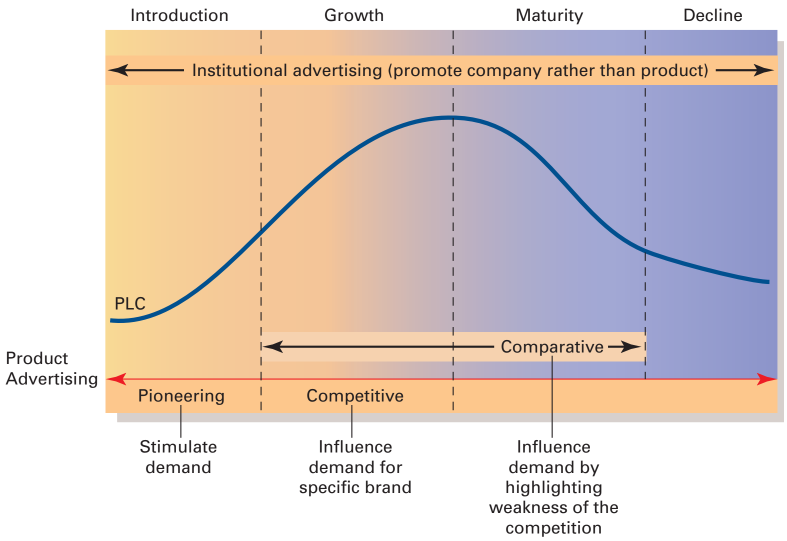
FTC rules also apply to advertisers making false claims about their own products. For example, the FTC recently filed a false-advertising suit against a company that marketed a weight-loss product which claimed that its users could lose substantial amounts of weight rapidly, including as much as 15 to 18 pounds per week and as much as 50 percent of all excess weight in just 14 days, without dieting or exercise. The company also included (false) assurances that clinical studies prove those claims.[14]

Companies must be careful with comparative advertising approaches in other countries as well. Germany, Italy, Belgium, and France, for example, do not permit advertisers to claim that their products are the best or better than competitors' products, both of which are common claims in the United States. In the Netherlands, car manufacturers cannot make claims in their advertising about the fuel consumption or environmental aspects of the car. Similarly, Lands' End ran afoul of a German law prohibiting lifetime guarantee claims, which happen to be one of Lands' End's guiding principles. The law has made it difficult for the direct retailer to sell its products and advertise its lifetime guarantee through the Internet and direct mail in Germany.

In other countries, hard-hitting comparative advertising will not be effective because it offends cultural values. For example, Arabic culture generally encourages people not to compete with one another, and the sharing of wealth is common practice. Therefore, comparative advertising is not consistent with social values in Arabic countries. Japanese advertisers have also been reluctant to use comparative advertising because it is considered confrontational and doesn't promote the respectful treatment of consumers or portray a company in a respectful light. Nevertheless, although the Japanese have traditionally favored soft-sell advertising approaches, consumers are witnessing a trend toward comparative ads.

REVIEW LEARNING OUTCOME

LO 2 Identify the major types of advertising



LO 3 Creative Decisions in Advertising

advertising campaign A series of related advertisements focusing on a common theme, slogan, and set of advertising appeals.

Advertising strategies typically are organized around an advertising campaign. An advertising campaign is a series of related advertisements focusing on a common theme, slogan, and set of advertising appeals. It is a specific advertising effort for a particular product that extends for a defined period of time. For example, Hewlett-Packard's celebrity-drenched global ad campaign, "The computer is personal again," helped HP gain the lead in worldwide market share for personal computers, and also imbued a once-faded brand with some cool. The glossy campaign, featuring print, video, and television ads, showcased achievers such as "CEO of Hip-Hop" Jay-Z, "Master of Snowboards" Shawn White, designer Vera Wang, and Brazilian author Paulo Coelho. Each celebrity was shown manipulating images that seemingly revolved around their laptop to show what's on their computer, what they do in their spare time, and why the PC is personal to them. A concurrent online campaign included a virtual motorcycle tour with the Orange County Choppers team, who were also the celebrity stars of HP's 2007 Super Bowl ad. That campaign was designed to create demand among 18 to 34 year olds for the HP Pavilion entertainment notebook and specially designed Orange County Choppers "skins," or computer covers.[15]

Before any creative work can begin on an advertising campaign, it is important to determine what goals or objectives the advertising should achieve. An advertising objective identifies the specific communication task that a campaign should accomplish for a specified target audience during a specified period. The objectives of a specific advertising campaign often depend on the overall corporate objectives and the product being advertised. For example, McIlhenny Company's Tabasco Hot Sauce launched a print advertising campaign with the objective of educating consumers about how to use the product and the variety of flavors offered. The ads featured product information embedded in the label, which was blown up to cover the entire page. The ad copy for the Garlic Pepper Sauce read: "The only one potent enough to ward off both hypothermia and vampires at once." The original Tabasco Pepper Sauce ad copy read: "It's like love, you always want more no matter how badly you got burned last time." The ad campaign increased sales by over 11 percent in the first four weeks. The print medium was also supported by participation in special events, such as the National Collegiate Tailgate Tour.[16]

advertising objective
A specific communication task that a campaign should accomplish for a specified target audience during a specified period.

The DAGMAR approach (Defining Advertising Goals for Measured Advertising Results) is one method of setting objectives. According to this method, all advertising objectives should precisely define the target audience, the desired percentage change in some specified measure of effectiveness, and the time frame in which that change is to occur. For example, the objectives for an advertising campaign for Coca-Cola's revamped POWERade brand might be to achieve a 15 percent increase in its share of the sports-drink market within eight months.

Once objectives are defined, creative work can begin on the advertising campaign. Advertising campaigns often follow the AIDA model, which was discussed in Chapter 16. Depending on where consumers are in the AIDA process, the creative development of an advertising campaign might focus on creating attention, arousing interest, stimulating desire, or ultimately leading to the action of buying the product. Specifically, creative decisions include identifying product benefits, developing and evaluating advertising appeals, executing the message, and evaluating the effectiveness of the campaign.

IDENTIFYING PRODUCT BENEFITS

A well-known rule of thumb in the advertising industry is "Sell the sizzle, not the steak"—that is, in advertising the goal is to sell the benefits of the product, not its attributes. An attribute is simply a feature of the product such as its easy-open package or special formulation. A benefit is what consumers will receive or achieve by using the product. A benefit should answer the consumer's question "What's in it for me?" Benefits might be such things as convenience, pleasure, savings, or relief. A quick test to determine whether you are offering attributes or benefits in your advertising is to ask "So?" Consider this example:

- *Attribute:* "SoBe Life Water has reformulated five delicious, low-calorie flavors—Blackberry Grape, Pomegranate Cherry, Orange Tangerine, Strawberry Kiwi and Passionfruit Citrus—each infused with a unique mix of antioxidant vitamins C & E, essential B vitamins and healthy herbal ingredients . . . " "So . . . ?"

- *Benefit*: "So . . . SoBe Life Water is not only an enhanced water; it is a lifestyle unto itself . . . providing consumers the healthiest, most fun and refreshing products, delivering the incredibly positive benefits of hydration and unmatched brand experiences."[17]

Marketing research and intuition are usually used to unearth the perceived benefits of a product and to rank consumers' preferences for these benefits. Coke's rival, PepsiCo, has its own sports drink, Gatorade. Already positioned as *the* thirst-quencher, Gatorade's advertising touts its refueling benefits to serious athletes of mainstream sports. Similarly, Kellogg's ad campaign for its latest cereal, Frosted Flakes Gold, has partnered with ESPN to promote the new frosted flake as a product that provides longer-lasting energy because it's a whole grain cereal. The ads underscore the message of increased, longer-lasting energy by featuring adolescent athletes being cheered on by Tony the Tiger.[18]

DEVELOPING AND EVALUATING ADVERTISING APPEALS

advertising appeal
A reason for a person to buy a product.

unique selling proposition
A desirable, exclusive, and believable advertising appeal selected as the theme for a campaign.

An **advertising appeal** identifies a reason for a person to buy a product. Developing advertising appeals, a challenging task, is typically the responsibility of the creative people in the advertising agency. Advertising appeals typically play off of consumers' emotions, such as fear or love, or address some need or want the consumer has, such as a need for convenience or the desire to save money.

Advertising campaigns can focus on one or more advertising appeals. Often the appeals are quite general, thus allowing the firm to develop a number of subthemes or minicampaigns using both advertising and sales promotion. Several possible advertising appeals are listed in Exhibit 17.2.

Choosing the best appeal from those developed normally requires market research. Criteria for evaluation include desirability, exclusiveness, and believability. The appeal first must make a positive impression on and be desirable to the target market. It must also be exclusive or unique; consumers must be able to distinguish the advertiser's message from competitors' messages. Most importantly, the appeal should be believable. An appeal that makes extravagant claims not only wastes promotional dollars but also creates ill will for the advertiser.

The advertising appeal selected for the campaign becomes what advertisers call its **unique selling proposition.** The unique selling proposition usually becomes the campaign's slogan. For example, Comfort Suites Hotels' newspaper ads feature a bright blue sky and the words "Fresh Air," to promote what they're calling one of their "best amenities"—100 percent smoke-free rooms.[19] POWERade's advertising campaign aimed at the sports enthusiast carries the slogan "Sport Is What You Make It." This is POWERade's unique selling proposition, implying that you can push yourself to the limit if you are motivated and use POWERade.[20]

Effective slogans often become so ingrained that consumers hearing the slogan immediately conjure up images of the product. For example, many consumers can easily name the companies and products behind these memorable slogans or even hum the jingle that goes along with them: "Have it your way," "Tastes great, less filling," "Ring around the collar," and "Tum

Exhibit 17.2
Common Advertising Appeals

Profit	Lets consumers know whether the product will save them money, make them money, or keep them from losing money
Health	Appeals to those who are body-conscious or who want to be healthy
Love or Romance	Is used often in selling cosmetics and perfumes
Fear	Can center around social embarrassment, growing old, or losing one's health; because of its power, requires advertiser to exercise care in execution
Admiration	Is the reason that celebrity spokespeople are used so often in advertising
Convenience	Is often used for fast-food restaurants and microwave foods
Fun and Pleasure	Are the key to advertising vacations, beer, amusement parks, and more
Vanity and Egotism	Are used most often for expensive or conspicuous items such as cars and clothing
Environmental Consciousness	Centers around protecting the environment and being considerate of others in the community

te Tum Tum." Advertisers often revive old slogans or jingles in the hope that the nostalgia will create good feelings with consumers. Maytag refreshed its campaign featuring its appliance pitchman by changing the actor who plays him and giving him a helper—the third change since the ads originated in 1967. And Hershey's Kit Kat bar's jingle "Gimme a Break" is so etched in consumers' minds that recently the agency hired a film crew to ask people on the street to sing the jingle for use on the Internet, in future ad campaigns, and in its Kit Kat "Gimme a Break" Café.[21]

EXECUTING THE MESSAGE

Message execution is the way an advertisement portrays its information. In general, the AIDA plan (see Chapter 16) is a good blueprint for executing an advertising message. Any ad should immediately draw the reader's, viewer's, or listener's attention. The advertiser must then use the message to hold interest, create desire for the good or service, and ultimately motivate action—a purchase.

The style in which the message is executed is one of the most creative elements of an advertisement. Exhibit 17.3 lists some examples of executional styles used by advertisers. Executional styles often dictate what type of media is to be employed to convey the message. Scientific executional styles lend themselves well to print advertising where more information can be conveyed. On the other hand, demonstration and musical styles are more likely found in broadcast advertising.

Testimonials by athletes are one of the more popular executional styles. Tiger Woods and Shaquille O'Neal are two of the most successful athlete spokespersons. Read Shaq's own words about the power of marketing and advertising in Exhibit 17.4.

Injecting humor into an advertisement is a popular and effective executional style. Selection of a humorous approach is based on the communications goal.

Exhibit 17.3

Ten Common Executional Styles for Advertising

Slice-of-Life	Depicts people in normal settings, such as at the dinner table or in their car. McDonald's often uses slice-of-life styles showing youngsters munching french fries and Happy Meals on family outings.
Lifestyle	Shows how well the product will fit in with the consumer's lifestyle. As their Volkswagen Jetta moves through the streets of the French Quarter, the Gen X drivers plug in a techno music CD and marvel at how the rhythms of the world mimic the ambient vibe inside their vehicle.
Spokesperson/ Testimonial	Can feature a celebrity, company official, or typical consumer making a testimonial or endorsing a product. Sarah Michelle Gellar, star of Buffy the Vampire Slayer, endorses Maybelline cosmetics while country singer Shania Twain introduced Revlon's ColorStay Liquid Lip. Dell, Inc. founder Michael Dell touts his vision of the customer experience via Dell in television ads.
Fantasy	Creates a fantasy for the viewer built around use of the product. Carmakers often use this style to let viewers fantasize about how they would feel speeding around tight corners or down long country roads in their cars.
Humorous	Advertisers often use humor in their ads, such as Snickers' "Not Going Anywhere for a While" campaign featuring hundreds of souls waiting, sometimes impatiently, to get into heaven.
Real/Animated Product Symbols	Creates a character that represents the product in advertisements, such as the Energizer bunny, Starkist's Charlie the Tuna, or General Mills' longtime icon, Betty Crocker, redesigned for the new millennium.
Mood or Image	Builds a mood or image around the product, such as peace, love, or beauty. De Beers ads depicting shadowy silhouettes wearing diamond engagement rings and diamond necklaces portrayed passion and intimacy while extolling that a "diamond is forever."
Demonstration	Shows consumers the expected benefit. Many consumer products use this technique. Laundry-detergent spots are famous for demonstrating how their product will clean clothes whiter and brighter. Fort James Corporation demonstrated in television commercials how its Dixie Rinse & ReUse disposable stoneware product line can stand up to the heat of a blowtorch and survive a cycle in a clothes washer.
Musical	Conveys the message of the advertisement through song. For example, Nike's ads depicting a marathoner's tortured feet, skier Picabo Street's surgery-scarred knee, and a surfer's thigh scarred by a shark attack while strains of Joe Cocker's "You Are So Beautiful" are heard in the background.
Scientific	Uses research or scientific evidence to give a brand superiority over competitors. Pain relievers like Advil, Bayer, and Excedrin use scientific evidence in their ads.

Exhibit 17.4

Dreamful Attraction: Shaquille O'Neal's Thoughts on Marketing and Advertising

While on the outside looking in, I did not realize that marketing was so complicated. I never knew that a person, such as an athlete, could have such a powerful effect on people's thought processes and purchasing behavior. The use of a well-known athlete in marketing a product or service can have a great impact on the sales of that product or service. Look at Michael Jordan. Almost overnight most every kid either was wearing or wanted to wear Air Jordan shoes.

Why does this happen? Is it the appeal of a great athlete or is it great marketing? The answer is "none of the above." It's both. In my years as a professional basketball player, I have seen firsthand the dramatic appeal that athletes have for the fans and public in general. Top-name athletes are like E. F. Hutton—when they talk, people listen. But why do they listen? I believe they listen to us, the athletes, because we have credibility. The effectiveness of celebrity endorsements depends largely on how credible and attractive the spokesperson is and how familiar people are with him or her. Companies sometimes use sports figures and other celebrities to promote products hoping they are appropriate opinion leaders.

Because of an athlete's fame and fortune, or attraction, the athlete can often have the right credibility to be a successful spokesperson. The best definition of credibility that I could find was by James Gordon in his book, Rhetoric of Western Thought. He said that attraction "can come from a person's observable talents, achievements, occupational position or status, personality and appearance, and style."* That may be why a famous athlete's personality and position can help him or her communicate more effectively than a not-so-famous athlete.

Credibility is a positive force in the persuasive promotion used predominantly by cola marketers like Pepsi because of what I like to call "dreamful attraction." For example, when I was young, I dreamed that I was like Dr. J., the famous basketball player for the Philadelphia 76ers. I would take his head off a poster and put my head on it. I wanted to be Dr. J. That is dreamful attraction. The youth of today are no different. Just the other day a kid stopped me and told me that he wanted to be like me. He had a dreamful attraction. This dreamful attraction can help sell products. In my case, Pepsi, Spalding, Kenner, and Reebok are hoping that they are able to package properly and market whatever dreamful attraction I might have for their target audience—kids.

There are many ways to communicate to my target audience. I find that the most effective way for me is through television commercials. This avenue gives me a chance to express myself and show my real feelings about a message we are trying to communicate—either visually or vocally. I feel that I have what Clint Eastwood has—"Sudden Impaq." My impact is revealed through my sense of humor and my nonverbal communication.

Why does Shaq sell? Communication. Although the verbal communication in many of my commercials is slim, the impact is still there. This makes me believe even more in the quote that who you are can almost be as important as what you say. But if you can blend the two together—who you are and what you have to say—then imagine how much more successful the communication message can be in the marketing process. Andre Agassi's favorite quote from his Canon commercial is "Image is everything." If it is not everything, it is almost everything. If you have the right image, match it with the right product, and market it properly, then success should follow.

I have been involved in commercials and the marketing of products for only a short time, but I have learned a great deal. If there is one formula for success in selling products, it would be this: Marketing plus credibility and image plus effective communications equals increase in sales—hopefully.

Now, you can call me Dr. Shaq, M.E. (Marketing Expert).

*James Gordon, *Rhetoric of Western Thought* (Dubuque, Iowa: Kendall-Hunt Publishing Co., 1976), 207.

Humorous executional styles are more often used in radio and television advertising than in print or magazine advertising where humor is less easily communicated. Regardless of the advertising medium, however, humor can be tricky to use because not all people find the same things funny and marketers have to be absolutely sure that the humor won't be misconstrued. For instance, a print and email ad campaign for Timbuk2's limited-edition messenger bags caused an uproar even while the ad's creators protested that it was supposed to be funny. The ad featured a photo of a crying girl in a prom dress next to a photo of a tough-looking guy across whom was written: "Here today. Gone tomorrow. Just like that jerk who stole your virginity, these bags are only around for a short time." Timbuk2 finally pulled the ad in response to a storm of negative blog postings and email protests against the ad saying that trying to be funny using a reference to date-rape was offensive.[22] Used appropriately, humor can be effective in attracting and holding audience attention. For example, Altoids used humor to create and reinforce its quirky yet strong persona. With a significantly lower budget than key competitors, the Altoids campaign helped the product grow from a sleepy brand to the number one mint in America based on flavor.[23]

Executional styles for foreign advertising are often quite different from those we are accustomed to in the United States. Sometimes they are sexually oriented or aesthetically imaginative. For example, adidas commissioned a German ad company to come up with a "talk-of-the-world, spectacular" outdoor ad to welcome visitors to the 2006 FIFA World Cup soccer match. They designed a 65-meter, front-and-back billboard of soccer star Oliver Kahn diving to catch a soccer ball, which stretched across a four-lane highway near the airport in Munich, Germany. Four million cars drove under the installation and it became the global visual that accompanied almost every foreign news coverage of the World Cup event.[24]

This "talk-of-the-world, spectacular" outdoor ad welcoming visitors to the 2006 FIFA World Cup soccer match is an example of an aesthetically imaginative executional style.

European advertising avoids the direct-sell approaches common in U.S. ads and instead is more indirect, more symbolic, and, above all, more visual. Nike, known in the United States for "in-your-face" advertising and irreverent slogans such as "Just Do It," discovered that its brash advertising did not appeal to Europeans.

Sometimes a company will modify its executional styles to make its advertising more effective. For decades, Procter & Gamble has advertised shampoo in China using a demonstrational executional style. Television ads demonstrated how the science of shampoo worked and then showed a woman with nice, shiny hair. Because today's urban Chinese customers are more financially secure, they no longer make solely utilitarian purchases. To reflect that shift, Procter & Gamble has begun incorporating more of an emotional appeal into its advertisements. A new set of TV ads shows a woman emerging from an animated cocoon as a sophisticated butterfly. A voice over says, "Head & Shoulders metamorphosis—new life for hair."[25] See the "Global Perspectives" box in this chapter for some other examples of advertising around the world.

POSTCAMPAIGN EVALUATION

Evaluating an advertising campaign can be the most demanding task facing advertisers. How do advertisers know whether the campaign led to an increase in sales or market share or elevated awareness of the product? Most advertising campaigns aim to create an image for the good or service instead of asking for action, so their real effect is unknown. So many variables shape the effectiveness of an ad that, in many cases, advertisers must guess whether their money has been well spent. Despite this gray area, marketers spend a considerable amount of time studying

GLOBAL Perspectives

Advertising Strategies Vary by Country

Global advertising positioning strategies use different tactics depending on the country. For example, China's ParkNshop, a discount retailer and supermarket, used animated shopping bags in a commercial. The commercial turns a typical shopping bag into an interactive shopping tool. To reinforce ParkNshop's image as a low-priced retailer, the bags in the commercial check the prices of the products before allowing them in the bag.

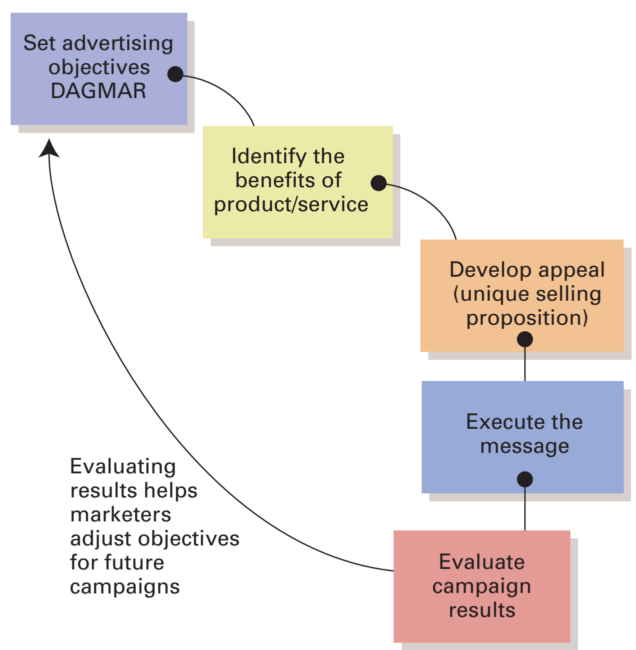
A Nokia advertising campaign for Australia, the Philippines, Vietnam, India, and China was designed to show consumers how a mobile phone can improve their lifestyles. The campaign, titled "We Never Stop Challenging the Future," was supported through TV, print, outdoor, and online advertising. One print ad showed a person stranded on a dirt road with the possibility of going in four different directions. The caption read "You could call for directions. Or use your phone to download maps. What if it could actually guide you home?" Another ad emphasized the phone's technological capabilities by showing a phone embedded in a man's hand. The copy read "First we took away the antenna. Then we made it smaller. What if we made it disappear?" Both ads focused on how mobility could enhance a consumer's lifestyle.

To build its image internationally, Volkswagen launched an emotion-based campaign. Aware that consumers already associate the brand with quality and reliability, Volkswagen wanted to capitalize on the feelings underlying those product attributes. In Germany, Volkswagen launched a multifaceted campaign using a 20-page magazine and newspaper insert and a TV commercial. Subsequent 2-page print ads featured a picture of a VW car and a poem about the feelings associated with a VW automobile. The intent was that consumers viewing these ads would identify with the emotions that support their beliefs about the company.[26]

These examples illustrate how companies are using advertising to reach consumers in markets outside the United States. How do the domestic advertising campaigns by the same companies differ? Compare the advertisements and consider the similarities and differences.

REVIEW LEARNING OUTCOME

LO 3 Discuss the creative decisions in developing an advertising campaign



advertising effectiveness and its probable impact on sales, market share, or awareness.

Testing ad effectiveness can be done either before or after the campaign. Before a campaign is released, marketing managers use pretests to determine the best advertising appeal, layout, and media vehicle. After advertisers implement a campaign, they often conduct tests to measure its effectiveness. Several monitoring techniques can be used to determine whether the campaign has met its original goals. Even if a campaign has been highly successful, advertisers still typically do a postcampaign analysis. They assess how the campaign might have been more efficient and what factors contributed to its success. For example, Hallmark's market researchers wanted to capitalize on aging baby boomers. Research indicated that baby boomers do not want to age, but since that is inevitable, boomers want to see the positive side of aging. Therefore, Hallmark created the "Time of Your Life" series that flattered their egos. The cards were not successful, however, because they were placed in the "over 50" section of the store and baby boomers do not want to shop in that section.[27]

LO 4

Media Decisions in Advertising

medium
The channel used to convey a message to a target market.

media planning
The series of decisions advertisers make regarding the selection and use of media, allowing the marketer to optimally and cost-effectively communicate the message to the target audience.

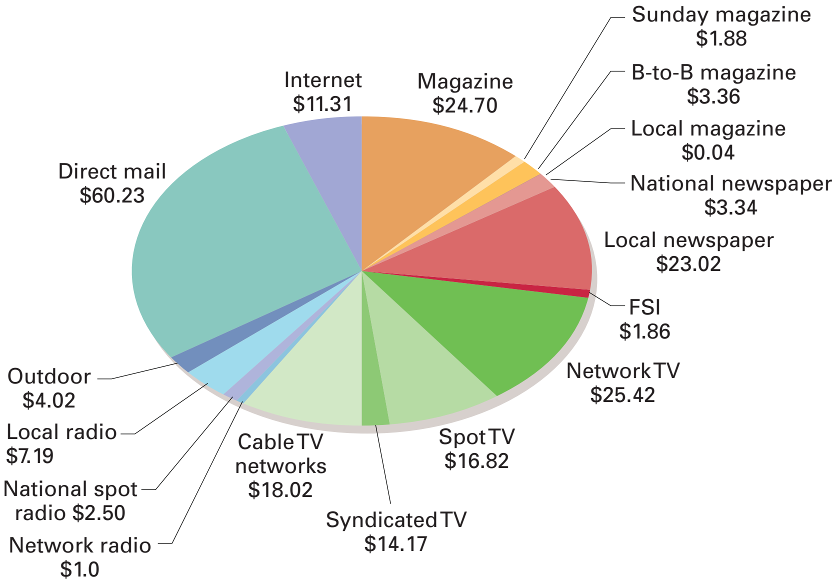
A major decision for advertisers is the choice of **medium**—the channel used to convey a message to a target market. **Media planning**, therefore, is the series of decisions advertisers make regarding the selection and use of media, allowing the marketer to optimally and cost-effectively communicate the message to the target audience. Specifically, advertisers must determine which types of media will best communicate the benefits of their product or service to the target audience and when and for how long the advertisement will run.

Promotional objectives and the appeal and executional style of the advertising strongly affect the selection of media. It is important to understand that both creative and media decisions are made at the same time. Creative work cannot be completed without knowing which medium will be used to convey the message to the target market. For instance, creative planning will likely differ for an ad to be displayed on a Web site versus one placed in a print medium, such as a newspaper or magazine. In many cases, the advertising objectives dictate the medium and the creative approach to be used. For example, if the objective is to demonstrate how fast a product operates, a TV commercial that shows this action may be the best choice.

U.S. advertisers spend about $300 billion on media advertising annually. Almost one-half of that is spent on media monitored by national reporting services—newspapers, magazines, Yellow Pages, Internet, radio, television, and outdoor media. The remainder is spent on unmonitored media, such as direct mail, trade exhibits, cooperative advertising, brochures, coupons, catalogs, and special events. Exhibit 17.5 shows advertising spending by media type. As you can see, about 44 percent of every media dollar goes toward TV ads, 20 percent toward direct mail, and about 18 percent for newspaper ads.[28] But these traditional mass-market media are declining in usage and more targeted media are growing.[29]

Exhibit 17.5

Domestic Advertising Spending by Media Type, in billions



SOURCE: "Total U.S. Advertising Spending by Medium," Special Report, June 23, 2008, Advertising Age, http://www.adage.com, accessed June 26, 2008.

MEDIA TYPES

Advertising media are channels that advertisers use in mass communication. The seven major advertising media are newspapers, magazines, radio, television, outdoor media, Yellow Pages, and the Internet. Exhibit 17.6 summarizes the advantages and disadvantages of these major channels. In recent years, however, alternative media vehicles have emerged that give advertisers innovative ways to reach their target audience and avoid advertising clutter.

Exhibit 17.6

Advantages and Disadvantages of Major Advertising Media

Medium	Advantages	Disadvantages
Newspapers	Geographic selectivity and flexibility; short-term advertiser commitments; news value and immediacy; year-round readership; high individual market coverage; co-op and local tie-in availability; short lead time	Little demographic selectivity; limited color capabilities; low pass-along rate; may be expensive
Magazines	Good reproduction, especially for color; demographic selectivity; regional selectivity; local market selectivity; relatively long advertising life; high pass-along rate	Long-term advertiser commitments; slow audience buildup; limited demonstration capabilities; lack of urgency; long lead time
Radio	Low cost; immediacy of message; can be scheduled on short notice; relatively no seasonal change in audience; highly portable; short-term advertiser commitments; entertainment carryover	No visual treatment; short advertising life of message; high frequency required to generate comprehension and retention; distractions from background sound; commercial clutter
Television	Ability to reach a wide, diverse audience; low cost per thousand; creative opportunities for demonstration; immediacy of messages; entertainment carryover; demographic selectivity with cable stations	Short life of message; some consumer skepticism about claims; high campaign cost; little demographic selectivity with network stations; long-term advertiser commitments; long lead times required for production; commercial clutter
Outdoor Media	Repetition; moderate cost; flexibility; geographic selectivity	Short message; lack of demographic selectivity; high "noise" level distracting audience
Internet	Fastest-growing medium; ability to reach a narrow target audience; relatively short lead time required for creating Web-based advertising; moderate cost	Difficult to measure ad effectiveness and return on investment; ad exposure relies on "click-through" from banner ads; not all consumers have access to the Internet

Newspapers

The advantages of newspaper advertising include geographic flexibility and timeliness. Because copywriters can usually prepare newspaper ads quickly and at a reasonable cost, local merchants can reach their target market almost daily. Because newspapers are generally a mass-market medium, however, they may not be the best vehicle for marketers trying to reach a very narrow market. For example, local newspapers are not the best media vehicles for reaching purchasers of specialty steel products or even tropical fish. These target consumers make up very small, specialized markets. Newspaper advertising also encounters a lot of distractions from competing ads and news stories; thus, one company's ad may not be particularly visible.

cooperative advertising
An arrangement in which the manufacturer and the retailer split the costs of advertising the manufacturer's brand.

The main sources of newspaper ad revenue are local retailers, classified ads, and cooperative advertising. In cooperative advertising, the manufacturer and the retailer split the costs of advertising the manufacturer's brand. One reason manufacturers use cooperative advertising is the impracticality of listing all their dealers in national advertising. Also, co-op advertising encourages retailers to devote more effort to the manufacturer's lines.

Magazines

Compared to the cost of other media, the cost per contact in magazine advertising is usually high. The cost per potential customer may be much lower, however, because magazines are often targeted to specialized audiences and thus reach more potential customers. The types of products most frequently advertised in magazines include automobiles, apparel, computers, and cigarettes.

One of the main advantages of magazine advertising is its market selectivity. Magazines are published for virtually every market segment. For instance, *Lucky* "The Magazine about Shopping and Style" is a leading fashion magazine; *ESPN the Magazine* is a successful sports magazine; *Essence* is targeted toward African American women; *Marketing News* is a trade magazine for the marketing professional; and *The Source* is a niche publication geared to young urbanites with a passion for hip-hop music.

In 2006, Philips Electronics began an innovative advertising campaign in select magazines by sponsoring the magazines' contents page. Issues of four Time Warner magazines (*Time, Fortune, People,* and *Business 2.0*) featured the table of contents on the first page rather than several pages later. The inside front cover features a Philips ad with the following copy: "Philips Electronics is bringing the table of contents to the front of selected Time, Inc. magazines to make things easier for readers." In general, the placement of the contents page varies from magazine to magazine, but it is not uncommon for the contents to appear after numerous advertisements; as many as 24 pages of ads can appear before a magazine's contents page. Philips paid Time, Inc., $5 million to sponsor the contents pages in the four magazines for only one issue each.[30]

Radio

Radio has several strengths as an advertising medium: selectivity and audience segmentation, a large out-of-home audience, low unit and production costs, timeliness, and geographic flexibility. Local advertisers are the most frequent users of radio advertising, contributing over three-quarters of all radio ad revenues. Like newspapers, radio also lends itself well to cooperative advertising.

Radio advertising is enjoying a resurgence in popularity. As Americans become more mobile and pressed for time, media such as network television and newspapers have lost viewers and readers, particularly in the youth market. Radio listening, however, has grown in step with population increases mainly because its immediate, portable nature meshes so well with a fast-paced lifestyle. The ability to target specific demographic groups is a major selling point for radio stations, attracting advertisers pursuing narrowly defined audiences that are more likely to respond to certain kinds of ads and products. Radio listeners also tend to listen habitually and at predictable times, especially during "drive time," when commuters form a vast captive audience. Finally, satellite radio has attracted new audiences that are exposed to ads when allowed on that format.

Television

Because television is an audiovisual medium, it provides advertisers with many creative opportunities. Television broadcasters include network television, independent stations, cable television, and a relative newcomer, direct broadcast satellite television. ABC, CBS, NBC, and the Fox Network dominate network television, which reaches a wide and diverse market. Conversely, cable television and direct broadcast satellite systems, such as DirecTV and Dish Network, offer consumers a multitude of channels devoted exclusively to particular audiences—for example, women, children, African Americans, nature lovers, senior citizens, Christians, Hispanics, sports fans, and fitness enthusiasts. Recent niche market entries include CSTV Network (college sports) and the NFL Network—focused exclusively on the sports enthusiast—and the casino and gambling channel. Because of its targeted channels, cable television is often characterized as "narrowcasting" by media buyers.

Advertising time on television can be very expensive, especially for network and popular cable channels. The top-ranked TV programs in recent years are aired on networks ABC, CBS, and Fox. The biggest draws are Fox's *American Idol and House;* ABC's *Dancing with the Stars, Samantha Who?, and Grey's Anatomy;* NBC's Sunday Night Football; and CBS's crime series, *CSI.*[31] First-run prime-time shows and special events command the highest rates for a typical 30-second spot, with the least expensive ads costing about $300,000 and the more expensive ones $500,000. Super Bowl spots are the most expensi ve—a 30-second spot during the 2008 Super Bowl telecast cost advertisers an average of $2.7 million.[32] The two dozen or so marketers paying such a premium price include typical big ad spenders such as Procter & Gamble, Anheuser-Busch, Coca-cola and FedEx. Most marketers consider the Super Bowl the "last bastion" of mass marketing available, with over $93 million viewers tuning in.[33]

COURTESY, ® SUPERBOWL 2009

One of the more successful recent television formats to emerge is the **infomercial,** a 30-minute or longer advertisement. Infomercials are an attractive advertising vehicle for many marketers because of the relatively inexpensive airtime and the lower production costs. Advertisers say the infomercial is an ideal way to present complicated information to potential customers, which other advertising vehicles typically don't allow time to do. Now a $200 billion-dollar industry, infomercials are increasingly being used by some mainstream marketers. Once relegated to late-night TV, infomercials are showing up in daytime fare, such as Fox's "The O'Reilly Factor," CBS's "60 Minutes" and CNBC's "Mad Money." Consumers who might have been skeptical of an ad's veracity on shopping networks, are less likely to suspect an ad shown during prime time television programs. A shorter direct-retail infomercial is more common in daytime programming, running an average of 120 seconds.[34]

infomercial
A 30-minute or longer advertisement that looks more like a TV talk show than a sales pitch.

Probably the most significant trend to affect television advertising is the rise in popularity of digital video recorders (DVRs) like TiVo. For every hour of television programming, an average of 15 minutes is dedicated to nonprogram material (ads, public service announcements, and network promotions), so it's hardly surprising that viewers weary of ad breaks have embraced ad-skipping DVR technology as the solution to interruptions during their favorite shows. Marketers of the products featured in those advertisements are not the only ones trying to figure out ways to keep consumers from avoiding them; networks are also concerned about ad skipping. If consumers are not watching advertisements, then marketers will spend a greater proportion of their advertising budgets on alternative media, and a critical revenue stream for networks will disappear. While NBC ran a test in 2006 to measure the effectiveness of running shorter blocks of advertising, the company also said that it has no intention of changing its business model relative to advertising sales. In late 2007, TiVo began offering interactive banner ads to advertisers, making those sponsors' names visible as their ads are being fast-forwarded. The full impact of DVR technology on television as an advertising medium has yet to be determined.[35]

Outdoor Media

Outdoor or out-of-home advertising is a flexible, low-cost medium that may take a variety of forms. Examples include billboards, skywriting, giant inflatables, mini-billboards in malls and on bus stop shelters, signs in sports arenas, lighted moving signs in bus terminals and airports, and ads painted on cars, trucks, buses, water towers, manhole covers, drinking glass coasters, and even people, called "living advertising." Students in London "rented" their foreheads for temporary tattoos of brands and then walked around specified areas of the city.[36] The plywood scaffolding that rings downtown construction sites can also carry ads. Manhattan's Times Square, with an estimated 1.5 million daily pedestrians, has been a popular area for outdoor advertising using scaffolding.

Outdoor advertising reaches a broad and diverse market and is, therefore, ideal for promoting convenience products and services as well as directing consumers to local businesses. One of outdoor's main advantages over other media is that its exposure frequency is very high, yet the amount of clutter from competing ads is very low. Outdoor advertising also has the ability to be customized to local marketing needs. For these reasons, local business establishments, such as local services and amusements, retailers, public transportation, and hotels and restaurants, are the leading outdoor advertisers. Outdoor advertising categories on the rise include telecommunications with a heavy emphasis on wireless services, financial services, and packaged goods.

Outdoor advertising is becoming more innovative. New technology is enabling outdoor ads to become interactive and to be more like online ads. For example, Nike commissioned a 23-story interactive, digital billboard on New York's Times Square. People passing the display on the sidewalk could use their cell phones to temporarily control the billboard and design their own shoes.[37] Virgin Atlantic Airways projected ads onto New York's and Chicago's skyscrapers, inviting passersby to access the airline's "Love From Above" campaign rewards.[38]

Unusual outdoor advertising campaigns are not limited to the United States. Adidas Japan created a "living billboard" in the form of a vertical soccer field on the side of a skyscraper. The billboard featured live players and a ball attached by ropes to the side of the building.[39] Virgin Atlantic painted an ad on the grass next to the runway at South Africa's Johannesburg International Airport to greet arriving and departing passengers. A world's first, the ad required 1,000 liters of paint and nine separate permits from different regulatory authorities due to the sensitive nature of the site.[40]

The Internet and Alternative Media Marketing

The Internet has definitely changed the advertising industry. With ad revenues reaching $25.5 billion in 2007, up 27 percent over 2006, the Internet has become a solid advertising medium. Online advertising continues to grow at double-digit rates—well ahead of other advertising media.[41] Researchers predict that by 2012, online ad spending will hit $61.3 billion and account for 18 percent of all marketing expenditures.[42] Internet advertising provides an interactive and versatile platform that offers rich data on consumer usage, enabling advertisers to improve their ad targetability and achieve measurable results.[43]

PR NEWSFOTO/© MICRO TARGET

Popular Internet sites and search engines, such as Google and Yahoo!, as well as online service providers like America Online, generally sell advertising space to marketers to promote their goods and services. Internet surfers click on these ads to be linked to more information about the advertised product or service. Established brands such as General Motors, Anheuser-Busch, Procter & Gamble, and Verizon have been adjusting their budgets to include Internet advertising, and other firms are not far behind. For example, Vonage, Circuit City, Ameritrade Brokerage, Amazon.com, Overstock.com, Netflix.com, and Monster.com have been among the top 50 advertisers on the Internet in recent years.

The effectiveness of Internet advertising has been hotly debated, however. Early research on banner ads found response rates as high as 30 percent, but more recent studies indicate much lower response rates. With high-speed broadband spreading rapidly in the United States, advertisers increasingly are switching to other approaches. For example, marketers are using ads that float, sing, or dance; video commercials similar to traditional TV spots; and ads that pop up in another window, use larger, hard-to-miss shapes, and include both online and offline cross-promotions. These new formats are often large enough for marketers to include their entire message so that users don't have to click through to another site.

Search Engine Ads One of the most popular approaches for Internet advertising is search engine ads. More than 113 billion searches were conducted in the U.S. in 2007 with Google getting the lion's share—nearly 64 billion.[44] In second place was Yahoo! with 2.2 billion searches, followed by Microsoft's MSN with 940 million.[45] Google's market share of Internet search has grown from 43 percent in 2005 to 56 percent in 2008.[46] Marketers' primary objective in using search engine ads is to enhance brand awareness. They do this through paid placement of ads tied to key words used in search engine searches—when someone clicks on the ad, the advertiser pays the search engine a fee.

advergaming
Placing advertising messages in Web-based or video games to advertise or promote a product, service, organization, or issue.

Advergaming Another popular Internet advertising format is advergaming. In advergaming, companies put ad messages in Web-based or video games to advertise or promote a product, service, organization, or issue. Sometimes the entire game amounts to a virtual commercial, other times advertisers sponsor games or buy ad space for product placement in them. Organizations using advergaming include Disney, Viacom's Nickelodeon, and even the U.S. Army.[47] The format encourages users to register for sweepstakes and other promotions and play the game. For example, a company with a heritage of aligning their products with gamers, Pepsi developed a multiplayer online game in which players get a chance to choose the next flavor of Mt. Dew. The site, dewmocracy.com, drew 700,000 unique visitors and 200,000 registered users who spent an average of 28 minutes per gaming session. Pepsi's "dewmocracy" advergame campaign taps into the explosive popularity of online connected game play, such as "World of Warcraft" with more than 10 million paying subscribers.[48]

An increasingly popular Internet advertising medium is social media marketing. Social media marketing is the collaboration and sharing of online content between the sender and the receiver—the brand and the consumer. The social media network, as one media pundit put it, is where word-of-mouth meets word-of-mouse . . . where authentic brands are rewarded and fake brands (and their empty promises) are punished."[49] Social media is sometimes referred to as user-generated content, or consumer-generated media, and includes blogs, podcasts, forums, interactive video tours, social networks, and virtual worlds.[50] This new way of using the Internet is possible (in part) because of Internet-driven technology such as RSS (Really Simple Syndication, or Rich Site Summary)—a data exchange format that provides Internet users with quick access to frequently updated online content such as blogs and news headlines.[51]

Blogging Initially, blogs had no advertising. But the popularity of some blogs has made them an attractive medium for marketing messages. Budget Rent-A-Car recently bought ads on 177 blogs, Audi of America paid for advertising on 286 blogs, and MSNBC bought ads on more than 800 blogs.[52] Seed Media, which produces science publications in print and online, sells advertising on its network of more than 15 blogs just as it does in its magazine *Seed*. Seed Media contends that by advertising on its blog network, marketers will gain access to a group of bright, curious consumers who buy all kinds of products.[53]

Podcasts Podcasts are audio or video shows on computers, portable MP3 players, or other Web-connected device. All that is needed to produce a podcast is a microphone connected to a computer and some audio software. Most consumer-users promote their "show" on a Web site or a blog and submit their podcast to podcast directories. Most major broadcasters now participate in podcasting. Apple's iTunes directory, for instance, offers NPR, ABC News, CNN, Comedy Central, MTV, The New York Times, and PBS podcasts.[54]

Advertainment

To cut through the clutter of traditional advertising media, advertisers are creating even more new media vehicles to advertise their products, some ordinary and others quite innovative. Alternative media vehicles can include shopping carts in grocery stores, computer screen savers, DVDs, interactive kiosks in department stores, advertisements run before movies at the cinema, and "advertainments"—"mini movies" that promote a product and are shown via the Internet.[55] For example, BMW shows films by recognized directors that run six to eight minutes and feature the cars in extreme situations.[56] Likewise, Coca-Cola sponsored a 25-minute advertainment program called "Sound Check" that was available only on TiVo. The program featured exclusive interviews, music videos, live shows, behind-the-scenes filming, and recordings by artists such as Ashanti, Sting, and Mary J. Blige.[57]

Indeed, almost anything can become a vehicle for displaying advertising. For instance, supermarkets have begun using "Flooranimation"—ads that are animated with graphics and sounds and installed on supermarket floors. Unanimated floor ads have been in use for some time, and research shows they increase sales 15 to 30 percent. Marketers are hoping that with animation and sound, sales will increase even more.[58] Billboards now include motion graphics, sound, and additional advertising media, are an excellent way to communicate with consumers in the evenings in metro markets such as New York City, Chicago, Los Angeles, and San Francisco.[59] Marketers are also looking for more innovative ways to reach captive and often bored commuters. For instance, subway systems now show ads via lighted boxes installed along tunnel walls. As a train passes through the tunnel, the passengers view the illuminated boxes, which create the same kind of illusion as a child's flip book, in which the images appear to move as the pages are flipped rapidly.

Video Game Advertising

When trying to reach males aged 18 to 34, video game advertising is emerging as an excellent medium, second only to prime-time *Monday Night Football*. The medium first attracted attention when Massive, Inc., (**http://www.massiveincorporated.com**) started a videogame advertising network and later established a partnership with Nielsen Entertainment, Inc., to provide ad ratings. Massive provides the capability to have ads with full motion and sound inserted into games played on Internet-connected computers. This is a big improvement over previous ads, which had to be inserted when the games were made and therefore quickly became obsolete. In 2006, Microsoft acquired Massive, a move that the company says will help it "deliver dynamic, relevant ads" across its online services including Xbox Live and MSN Games.[60]

Cell phones

Cell phones are among the newest advertising media and are particularly useful for reaching the youth market. Mobile advertising has incredible upside potential when you consider that there are more than 3 billion cell phone users in the world. In 2006, cell phone advertising sales reached over $400 million in the U.S. and nearly $900 million worldwide. Mobile ad spending is expected to grow to nearly $15 billion worldwide by 2011.[61] Today's data- and video-oriented phones can deliver advertisements and also have GPS capability, so they can receive "location-based" advertising; for example, a nearby restaurant can alert potential customers about specials. McDonald's enjoyed success doing this at locations in California where it gave away free McFlurry desserts. Marketers also are using text and video messages to notify customers of special deals, such as ring tone downloads. Cell phone advertising is less popular in the United States than in Europe and Asia, where cell phone owners use text messaging much more heavily. Although there is concern that cell phone spam will become as much of a problem as Internet spam, cell phone advertisers are targeting their ads to users who agree to receive the ads in exchange for premium services or who sign up on opt-in lists to learn about items that interest them, such as a particular band's next album or concert.[62]

Stealth Marketing The term "stealth" might conjure images of undercover operations, possibly even sneakiness. In marketing, however, stealth has come to mean a campaign of outsmarting the competition, rather than outspending them. Stealth marketing, also known as guerrilla marketing, or buzz, is usually just any unconventional way of performing marketing promotions on a low budget. Stealth marketing is often designed to leave the target audience unaware they have been marketed to, but that they have simply participated in something fun, or sometimes shocking. For instance, in a recent guerilla campaign promoting the film "The Water Horse: Legend Of the Deep" a 50-foot dragon (think Loch Ness monster) was created by way of hologram projection on the water surface of Tokyo bay, in Japan. Conjuring a huge monster practically out of thin air created marketing "buzz" online, on the street, and in the media.[63]

MEDIA SELECTION CONSIDERATIONS

media mix
The combination of media to be used for a promotional campaign.

cost per contact
The cost of reaching one member of the target market.

reach
The number of target consumers exposed to a commercial at least once during a specific period, usually four weeks.

frequency
The number of times an individual is exposed to a given message during a specific period.

audience selectivity
The ability of an advertising medium to reach a precisely defined market.

An important element in any advertising campaign is the media mix, the combination of media to be used. Media mix decisions are typically based on several factors: cost per contact, reach, frequency, target audience considerations, flexibility of the medium, noise level, and the life span of the medium.

Cost per contact is the cost of reaching one member of the target market. Naturally, as the size of the audience increases, so does the total cost. Cost per contact enables an advertiser to compare media vehicles, such as television versus radio or magazine versus newspaper, or more specifically *Newsweek* versus *Time*. An advertiser debating whether to spend local advertising dollars for TV spots or radio spots could consider the cost per contact of each. The advertiser might then pick the vehicle with the lowest cost per contact to maximize advertising punch for the money spent.

Reach is the number of different target consumers who are exposed to a commercial at least once during a specific period, usually four weeks. Media plans for product introductions and attempts at increasing brand awareness usually emphasize reach. For example, an advertiser might try to reach 70 percent of the target audience during the first three months of the campaign. Reach is related to a medium's ratings, generally referred to in the industry as *gross ratings points*, or GRP. A television program with a higher GRP means that more people are tuning in to the show and the reach is higher. Accordingly, as GRP increases for a particular medium, so does cost per contact.

Because the typical ad is short-lived and because often only a small portion of an ad may be perceived at one time, advertisers repeat their ads so that consumers will remember the message. Frequency is the number of times an individual is exposed to a message during a specific period. Advertisers use average frequency to measure the intensity of a specific medium's coverage. For example, Coca-Cola might want an average exposure frequency of five for its POWERade television ads. That means that each of the television viewers who saw the ad saw it an average of five times.

Media selection is also a matter of matching the advertising medium with the product's target market. If marketers are trying to reach teenage females, they might select *Seventeen* magazine. If they are trying to reach consumers over 50 years old, they may choose *Modern Maturity* magazine. A medium's ability to reach a precisely defined market is its audience selectivity. Some media vehicles, like general newspapers and network television, appeal to a wide cross section of the population. Others—such as *Brides, Popular Mechanics, Architectural Digest, Lucky,* MTV, ESPN, and Christian radio stations—appeal to very specific groups.

The *flexibility* of a medium can be extremely important to an advertiser. In the past, because of printing timetables, paste-up requirements, and so on, some magazines required final ad copy several months before publication. Therefore, magazine advertising traditionally could not adapt as rapidly to changing market conditions. While this is fast changing due to computer technology that creates electronic ad images and layouts, the lead time for magazine advertising is still considerably longer. Radio and Internet advertising, on the other hand, provide maximum flexibility. Usually, the advertiser can change a radio ad on the day it is aired, if necessary. Similarly, advertisements on the Internet can be changed in minutes with the click of a few buttons.

Noise level is the level of distraction associated with a medium. For example, to understand a televised promotional message, viewers must watch and listen carefully. But they often watch television with others, who may well provide distractions. Noise can also be created by competing ads, as when a street is lined with billboards or when a television program is cluttered with competing ads. About two-thirds of a newspaper's pages are now filled with advertising. A recent Sunday issue of the *Los Angeles Times* contained over one thousand ads, not counting the small classifieds. Even more space is dedicated to ads in magazines. For example, 85 percent of the space in the February/March issue of *Brides* magazine is typically devoted to advertisements. In contrast, direct mail is a private medium with a low noise level. Typically, no other advertising media or news stories compete for direct-mail readers' attention.

Media have either a short or a long life span. *Life span* means that messages can either quickly fade or persist as tangible copy to be carefully studied. For example, a radio commercial may last less than a minute. Listeners can't replay the commercial unless they have recorded the program. One way advertisers overcome this problem is by repeating radio ads often. In contrast, a magazine has a relatively long life span. A person may read several articles, put the magazine down, and pick it up a week later to continue reading. In addition, magazines often have a high pass-along rate. That is, one person will read the publication and then give it to someone else to read.

Media planners have traditionally relied on the above factors for selecting an effective media mix, with reach, frequency, and cost often the overriding criteria. Some experts, however, question the reliance media planners have traditionally placed on reach and frequency. For instance, well-established brands with familiar messages probably need fewer exposures to be effective, while newer brands or brands with unfamiliar messages likely need more exposures to become familiar.

Additionally, media planners have hundreds more media options today than they had 40 years ago when network television reigned. For instance, there are over 1,600 television stations across the country. In the Los Angeles market alone, there are now 79 radio stations, with 7 offering an "adult contemporary" format. The number of unique magazine titles has more than doubled over the last decade, with publications now targeting every possible market segment. Satellite television can now bring hundreds of channels into viewers' homes. The Internet provides media planners with even more targeted choices in which to send their messages. And alternative media choices are popping up in some very unlikely places. *Media fragmentation* is forcing media planners to pay as much attention to where they place their advertising, as to how often the advertisement is repeated. Indeed, experts recommend evaluating reach along with frequency in assessing the effectiveness of advertising. That is, in certain situations it may be important to reach potential consumers through as many media vehicles as possible. When this approach is considered, however, the budget must be large enough to achieve sufficient levels of frequency to have an impact. In evaluating reach versus frequency, therefore, the media planner ultimately must select an approach that is most likely to result in the ad being understood and remembered when a purchase decision is being made.

Advertisers also evaluate the qualitative factors involved in media selection. These qualitative factors include such things as attention to the commercial and the program, involvement, lack of distractions, how well the viewer likes the program, and other audience behaviors that affect the likelihood that a commercial message is being seen and, hopefully, absorbed. While advertisers can advertise their product in as many media as possible and repeat the ad as many times as they like, the ad still may not be effective if the audience is not paying attention. Research on audience attentiveness for television, for example, shows that the longer viewers stay tuned to a particular program, the more memorable they find the commercials. Holding power, therefore, can be more important than ratings (the number of people tuning in to any part of the program) when selecting media vehicles, challenging the long-held assumption that the higher the rating of a program, the more effective the advertising run during the program, even though it is more costly. For instance, *ER,* one of the top-rated shows among 25- to 54-year-olds, costs about $400,000 for a 30-second spot but ranks relatively low for holding power. In contrast, the low-rated *Candid Camera,* which ranks high in holding power, costs only about $55,000 for a 30-second spot.[64]

MEDIA SCHEDULING

media schedule
Designation of the media, the specific publications or programs, and the insertion dates of advertising.

continuous media schedule
A media scheduling strategy in which advertising is run steadily throughout the advertising period; used for products in the latter stages of the product life cycle.

flighted media schedule
A media scheduling strategy in which ads are run heavily every other month or every two weeks, to achieve a greater impact with an increased frequency and reach at those times.

pulsing media schedule
A media scheduling strategy that uses continuous scheduling throughout the year coupled with a flighted schedule during the best sales periods.

seasonal media schedule
A media scheduling strategy that runs advertising only during times of the year when the product is most likely to be used.

After choosing the media for the advertising campaign, advertisers must schedule the ads. A **media schedule** designates the medium or media to be used (such as magazines, television, or radio), the specific vehicles (such as *People* magazine, the show *Lost* on TV, or the American Top 40 national radio program), and the insertion dates of the advertising.

There are three basic types of media schedules:

- Products in the latter stages of the product life cycle, which are advertised on a reminder basis, use a **continuous media schedule.** A continuous schedule allows the advertising to run steadily throughout the advertising period. Examples include Ivory soap, Tide detergent, Bounty paper towels, and Charmin toilet tissue, which may have an ad in the newspaper every Sunday and a TV commercial on NBC every Wednesday at 7:30 P.M. over a three-month time period.
- With a **flighted media schedule,** the advertiser may schedule the ads heavily every other month or every two weeks to achieve a greater impact with an increased frequency and reach at those times. Movie studios might schedule television advertising on Wednesday and Thursday nights, when moviegoers are deciding which films to see that weekend. A variation is the **pulsing media schedule,** which combines continuous scheduling with flighting. Continuous advertising is simply heavier during the best sale periods. A retail department store may advertise on a year-round basis but place more advertising during certain sale periods such as Thanksgiving, Christmas, and back-to-school.
- Certain times of the year call for a **seasonal media schedule.** Products like Contac cold tablets and Coppertone suntan lotion, which are used more during certain times of the year, tend to follow a seasonal strategy. Advertising for champagne is concentrated during the weeks of Christmas and New Year's, whereas health clubs concentrate their advertising in January to take advantage of New Year's resolutions.

New research comparing continuous media schedules and flighted ones finds that continuous schedules for television advertisements are more effective than flighting in driving sales. The research suggests that it may be more important to get exposure as close as possible to the time when someone is going to make a purchase. For example, if a consumer shops on a weekly basis, the best time to reach that person is right before he or she shops. Therefore, the advertiser should maintain a continuous schedule over as long a period of time as possible. Often called *recency planning,* this theory of scheduling is now commonly used for scheduling television advertising for frequently purchased products, such as Coca-Cola or Tide detergent. Recency planning's main premise is that advertising works by influencing the brand choice of people who are ready to buy.

REVIEW LEARNING OUTCOME

LO4 Describe media evaluation and selection techniques

Media Choices

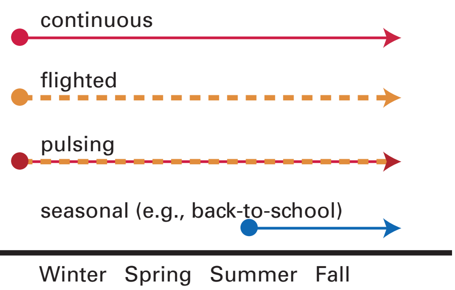
Type:

Considerations:

Mix	**(How much of each?)**
Cost per contact	**(How much per person?)**
Reach	**(How many people?)**
Frequency	**(How often?)**
Audience selectivity	**(How targeted is audience?)**

flexibility
noise
life span
fragmentation

Scheduling:



LO5 Public Relations

Public relations is the element in the promotional mix that evaluates public attitudes, identifies issues that may elicit public concern, and executes programs to gain public understanding and acceptance. Like advertising and sales promotion, public relations is a vital link in a progressive company's marketing communication mix. Marketing managers plan solid public relations campaigns that fit into overall marketing plans and focus on targeted audiences. These campaigns strive to maintain a positive image of the corporation in the eyes of the public. Before launching public relations programs, managers evaluate public attitudes and company actions. Then they create programs to capitalize on the factors that enhance the firm's image and minimize the factors that could generate a negative image.

In recent years, fast-food companies like McDonald's and soft drink companies like Coca-Cola have been criticized for contributing to childhood obesity, particularly in the United States. In response, the companies have undertaken public relations campaigns to try to minimize the impact on their reputations and ultimately sales. For example, Coca-Cola created the Beverage Institute for Health and Wellness to support nutrition research, education, and outreach. The company also spent $4 million to develop the "Live It" children's fitness campaign in schools across the country. Coke's nutrition communication manager says the campaign will not address childhood obesity or encourage students to drink Coke and that the company's logo will not appear on "Live It" materials. In addition to promoting the campaign, Coke is paying for campaign posters, pedometers, and nutrition education materials and offering prizes to children who meet the program's exercise goal of walking 10,000 steps in a week. Such efforts are designed to offset a push by the Center for Science in the Public Interest to persuade the Food and Drug Administration to require labels on sodas warning about obesity, tooth decay, and diabetes.[65]

A public relations program can generate favorable **publicity**—public information about a company, product, service, or issue appearing in the mass media as a new item. Organizations generally do not pay for the publicity and are not identified as the source of the information, but they can benefit tremendously from it. For example, the rapid growth of the satellite radio industry is partly due to publicity. Subscribers topped 12 million in 2005 and were expected to reach 15 million in 2006. Satellite radio's profile received a huge boost from the storm of publicity surrounding the decision by the country's most notorious and popular radio host, "shock jock" Howard Stern, to quit CBS radio and join censor-free Sirius satellite radio. Stern's first satellite broadcast was a major event, with the national media breathlessly reporting on the number of times he swore and looking for acceptable ways to report the more graphic—usually sexual—content of the show. After signing

public relations
The marketing function that evaluates public attitudes, identifies areas within the organization the public may be interested in, and executes a program of action to earn public understanding and acceptance.

publicity
Public information about a company, product, service, or issue appearing in the mass media as a news item.

Howard Stern quit CBS radio and joined censor-free Sirius satellite radio, Sirius's subscriber base mushroomed from 600,000 to over 3.5 million in one year.

© AP PHOTO/GREGORY BULL

Stern, Sirius's subscriber base mushroomed from 600,000 to over 3.5 million in one year—the majority of new listeners were Stern fans who signed up to follow their hero. Although Sirius added Stern, XM Satellite Radio still has more subscribers at around 9 million. XM also benefited from the publicity Stern generated for the whole satellite broadcast medium and generated publicity of its own by signing up both Oprah Winfrey and reclusive music legend Bob Dylan to host their own shows.[66]

Again, although organizations do not directly pay for publicity, it should not be viewed as free. Preparing news releases, staging special events, and persuading media personnel to broadcast or print publicity messages costs money. Public relations departments may perform any or all of the following functions:

- *Press relations:* placing positive, newsworthy information in the news media to attract attention to a product, a service, or a person associated with the firm or institution
- *Product publicity:* publicizing specific products or services
- *Corporate communication:* creating internal and external messages to promote a positive image of the firm or institution
- *Public affairs:* building and maintaining national or local community relations
- *Lobbying:* influencing legislators and government officials to promote or defeat legislation and regulation
- *Employee and investor relations:* maintaining positive relationships with employees, shareholders, and others in the financial community
- *Crisis management:* responding to unfavorable publicity or a negative event

MAJOR PUBLIC RELATIONS TOOLS

Public relations professionals commonly use several tools, including new-product publicity, product placement, consumer education, sponsorship, and Web sites. Although many of these tools require an active role on the part of the public relations professional, such as writing press releases and engaging in proactive media relations, some techniques create their own publicity.

New-Product Publicity

Publicity is instrumental in introducing new products and services. Publicity can help advertisers explain what's different about their new product by prompting free news stories or positive word of mouth about it. During the introductory period, an especially innovative new product often needs more exposure than conventional, paid advertising affords. Public relations professionals write press releases or develop videos in an effort to generate news about their new product. They also jockey for exposure of their product or service at major events, on popular television and news shows, or in the hands of influential people.

product placement
A public relations strategy that involves getting a product, service, or company name to appear in a movie, television show, radio program, magazine, newspaper, video game, video or audio clip, book, or commercial for another product; on the Internet; or at special events.

Product Placement

Marketers are increasingly using product placement to reinforce brand awareness and create favorable attitudes. Product placement is a strategy that involves getting one's product, service, or name to appear in a movie, television show, radio program, magazine, newspaper, video game, video or audio clip, book, or commercial for another product; on the Internet; or at special events. Including an actual product such as a can of Pepsi adds a sense of realism to a movie, TV show, video game, book, or similar vehicle that a can simply marked "soda" cannot. Product placements are arranged through barter (trade of product for placement), through paid placements, or at no charge when the product is viewed as enhancing the vehicle where it is placed.

Product placement expenditures amount to about $5 billion annually. Though this amount is small relative to other marketing expenditures, it is growing rapidly due to increasing audience fragmentation and the spread of ad-skipping technology, and continues to grow at about 30 percent per year.[67] More than two-thirds of product placements are in movies and TV shows, but placements in alternative media are growing, particularly on the Internet and in video games. Most product placements are for transportation, clothing, food, beverages, home furnishings, travel, and leisure time activities. Companies like BMW, Lexus, Coca-Cola, Pepsi, Procter & Gamble, and Hershey have frequently used product placement as a public relations strategy. Indeed, Pepsi appeared in seven top-ranked films in one year. Digital technology now enables companies to "virtually" place their products in any audio or video production. Virtual placement not only reduces the cost of product placement for new productions but also enables companies to place products in previously produced programs, such as reruns of television shows and movies.

Companies obtain valuable product exposure, brand reinforcement, and increased sales through product placement, often at a much lower cost than in mass media like television ads. For example, Burger King products were woven into *The Apprentice* when contestants wore Burger King uniforms and flipped burgers as part of a challenge; Ford sponsored the show *24*, with the main character, Jack Bauer, driving a Ford Expedition; and S.C. Johnson placed the ant killer RAID in an episode of the popular HBO series *The Sopranos*. When Red Stripe, a Jamaican-brewed beer, appeared in the movie *The Firm,* its U.S. sales increased more than 50 percent in the first month after the movie was released.[68]

Consumer Education

Some major firms believe that educated consumers are better, more loyal customers. BMW of North America, for example, sponsored an instructional driving school for teenagers in major cities across the United States. Teens received a special four-hour training session that included driving techniques, accident avoidance skills, and traction aid tricks from a professional driver. Financial planning firms often sponsor free educational seminars on money management, retirement planning, and investing in the hope that the seminar participants will choose the sponsoring organization for their future financial needs. Likewise, computer hardware and software firms, realizing that many consumers are intimidated by new technology and recognizing the strong relationship between learning and purchasing patterns, sponsor computer seminars and free in-store demonstrations.

Sponsorships

Sponsorships are increasing both in number and as a proportion of companies' marketing budgets, with worldwide sponsorship spending expected to exceed $30 billion in 2006. Probably the biggest reason for the increasing use of sponsorships is the difficulty of reaching audiences and differentiating a product from competing brands through the mass media. With a **sponsorship,** a company spends money to support an issue, cause, or event that is consistent with corporate objectives, such as improving brand awareness or enhancing corporate image. Most commonly, companies sponsor events such as festivals and fairs, conventions, expositions, sporting events, arts and entertainment spectaculars, and charity benefits. Typical examples of sponsorships include Jose Cuervo Tequila's sponsorship of the 2006

sponsorship
A public relations strategy in which a company spends money to support an issue, cause, or event that is consistent with corporate objectives, such as improving brand awareness or enhancing corporate image.

PR NEWSFOTO/© NIKE GOLF

Pro Beach Volleyball Tour, Domino's Pizza's sponsorship of Michael Waltrip for the 2006 NASCAR season, Hilton Hotels' sponsorship of the Hilton Family Skating & Gymnastics Spectacular 2006 on NBC, Levi Strauss & Co.'s partnership with the San Francisco Giants to sponsor the right field section of the park to be named "Levi's Landing," and Anheuser-Busch's Bud Bowl 2006 that featured hip-hop star Snoop Dogg and rock band 3 Doors Down.[69]

Although companies have recently been turning to specialized events such as tie-ins with schools, charities, and other community service organizations, the most popular sponsorship events are still those involving sports, music, or the arts. For example, Vodafone, Coca-Cola, Saturn, Michelin, and Yamaha were among the sponsors of the 2005 Gravity Games extreme sporting event in Perth, Australia, which competes with ESPN's XGames. More than 55,000 people attended the games to watch 110 of the world's biggest names in action sports participate in freestyle motocross, skateboarding, wakeboarding, BMX, and aggressive in-line skating. Sponsors distributed free samples, hosted extreme athlete autograph sessions and sports demonstrations, and organized alternative music concerts.[70] Likewise, McDonald's expanded its "I'm lovin' it" campaign to include sponsorships of NASCAR, the Pro Beach Volleyball Tour, and the Big Mac Challenge—a 20-stop lifestyle-oriented car show including DJs and other youth-focused activities. Similarly, Yahoo! sponsored a video game tour to promote Yahoo! Music Unlimited, Napster forged a deal with the Dew Action Sports Tour, and MSN Music hosted Milwaukee's Summerfest and Manchester, Tennessee's Bonnaroo Music and Arts Festival.[71]

Marketers sometimes create their own events tied around their products. The state of Hawaii organized its own mall touring event, titled "Experience Aloha: Hawaii on Tour," to promote the islands as a tourist destination. The tour traveled to 22 U.S. cities for weekend mall visits that included hula dancers, chefs cooking Hawaiian cuisine, lei-making demonstrations, and a virtual reality film simulating a helicopter ride over Hawaii's islands. Many other states also sponsor events promoting tourism.

Corporations sponsor issues as well as events. Sponsorship issues are quite diverse, but the three most popular are education, health care, and social programs. Firms often donate a percentage of sales or profits to a worthy cause favored by their target market.

cause-related marketing
A type of sponsorship involving the association of a for-profit company and a nonprofit organization; through the sponsorship, the company's product or service is promoted, and money is raised for the nonprofit.

A special type of sponsorship, cause-related marketing, involves the association of a for-profit company with a nonprofit organization. Through the sponsorship, the company's product or service is promoted, and money is raised for the nonprofit. In a common type of cause-related sponsorship, a company agrees to donate a percentage of the purchase price of a particular item to a charity, but some arrangements are more complex. In the United Kingdom, for example, Blockbuster Entertainment Ltd. works with Starlight Children's Foundation to raise money, and Tesco supermarkets raise money for computers in schools. Similarly, in the United States Avon, Yoplait Yogurt, and BMW support the Susan G. Komen Breast Cancer Foundation, and J. P. Morgan Chase & Co. Bank works with St. Jude Children's Research Hospital. Findings from several studies suggest that some consumers onsider a company's reputation when making purchasing decisions and that a company's community involvement boosts employee morale and loyalty.[72]

Internet Web Sites

Companies increasingly are using the Internet in their public relations strategies. Company Web sites are used to introduce new products, promote existing products, obtain consumer feedback, post news releases, communicate legislative and regulatory information, showcase upcoming events, provide links to related sites, release financial information, and perform many more marketing activities. Online reviews from opinion leaders and other consumers help marketers sway purchasing decisions in their favor. On its Web site for Playstation3 (**http://www.playstation.com**), Sony has online support, events and promotions, game trailers, and new and updated product releases such as Bode Miller Alpine Skiing 2007, King Kong, Madden NFL 07, Playboy Mansion and Jak X: Combat Racing. The site also includes message boards where the gaming community posts notes and chats, exchanges tips on games, votes on lifestyle issues like music and videos, and learns about promotional events.[73]

Web sites are also being incorporated into integrated marketing communications strategies. For example, CBS integrated broadcast advertising with product placement by placing a bonus scene from *CSI: Miami* on its Web site featuring a plot twist that was not revealed to television viewers until later in the season. The bonus scene page was sponsored by General Motors' Hummer brand, which also appeared in the bonus scene itself.[74]

More and more often, companies are also using blogs—both corporate and noncorporate—as a tool to manage their public images. Noncorporate blogs cannot be controlled, but marketers must monitor them to be aware of and respond to negative information and encourage positive content. Wal-Mart has been especially active in cultivating bloggers to get the company's message out. Mona Williams, Wal-Mart's spokeswoman, says, "We reach out to bloggers in the same way we reach out to reporters. A lot of people are looking to bloggers for their news source, and this is a good way to get our message out."[75] The company has enlisted the services of a public relations firm to help it combat negative publicity. The publicist assigned to the Wal-Mart account, Marshall Manson, contacts bloggers who write pro-Wal-Mart content and asks if he can send them materials to use in their commentaries. Those who agree become champions for the giant retailer.[76]

In addition to "getting the message out," companies are using blogs to create communities of consumers who feel positively about the brand. The hope is that the positive attitude toward the brand will build into strong word-of-mouth marketing. Companies must exercise caution when diving into corporate blogging, however. Coca-Cola launched a blog authored by a fictional character that did little except parrot the company line. Consumers immediately saw the blog for what it was (a transparent public relations platform) and lambasted Coca-Cola for its insincerity.[77]

crisis management
A coordinated effort to handle all the effects of unfavorable publicity or of another unexpected unfavorable event.

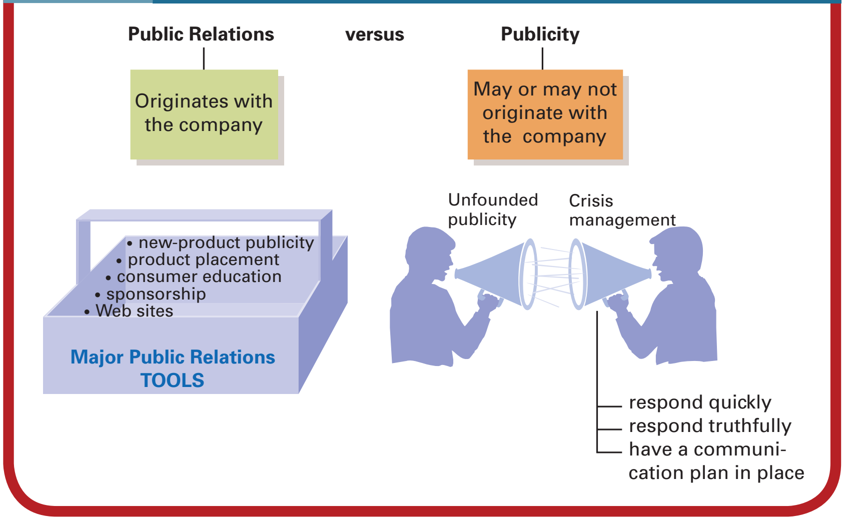
MANAGING UNFAVORABLE PUBLICITY

Although marketers try to avoid unpleasant situations, crises do happen. In our free-press environment, publicity is not easily controlled, especially in a crisis. Crisis management is the coordinated effort to handle the effects of unfavorable publicity, ensuring fast and accurate communication in times of emergency.

A good public relations staff is as important in bad times as in good. Companies must have a communication policy firmly in hand before a disaster occurs, because timing is uncontrollable. For example, in 2004, McDonald's was caught off-guard by the wave of negative publicity that followed the release of *Super Size Me*, a documentary film which chronicled the deterioration of filmmaker Morgan Spurlock's health while he experimented with an all-McDonald's diet. Two years later, in anticipation of a similar response to the movie version of Eric Schlosser's best seller *Fast Food*

REVIEW LEARNING OUTCOME

LO5 Discuss the role of public relations in the promotional mix



Nation, McDonald's contemplated dispatching a "truth squad" and a team of "ambassadors of the brand" to remind consumers that the restaurant offers a healthy menu and provides good jobs. The company has modified its menu to include more salads and apple dippers. McDonald's hopes new marketing communication focused on the importance of a balanced lifestyle will override any negative publicity resulting from the newer documentary.[78]

When Wal-Mart became the target of negative publicity regarding its low wages and sparse benefits, publicist Marshall Manson sent a special missive to his network of bloggers. It revealed that various unions were hiring the homeless and day laborers to protest at nonunion businesses, including Wal-Mart. The unions paid the picketers minimum wage and gave them no benefits. Manson's release was used by numerous bloggers and represented a counterattack in the publicity war over Wal-Mart's employment practices.[79]

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worldwide advertising expenditures in 2008 > **$480 billion**

$900,000 < people employed in media advertising

hours of commercial television messages the average viewer sees each week > **6**

cost of Pfizer's recent advertising campaign for the fibromyalgia medication Lyrica > **$46 million**

meters on the front-and-back adidas billboard welcoming visitors to the 2006 FiFA World Cup soccer match > **65**

120 < seconds in the average direct-retail daytime infomercial

daily pedestrians in Manhattan's Time's Square > **1.5 million**

113 billion < Internet searches conducted in the U.S. in 2007

percentage of the February/March issue of *Brides* magazine devoted to ads > **85**

1,600 < television stations in the U.S.

Review and Applications

LO 1

Discuss the effects of advertising on market share and consumers. Advertising helps marketers increase or maintain brand awareness and, subsequently, market share. Typically, more is spent to advertise new brands with a small market share than to advertise older brands. Brands with a large market share use advertising mainly to maintain their share of the market. Advertising affects consumers' daily lives as well as their purchases. Although advertising can seldom change strongly held consumer attitudes and values, it may transform a consumer's negative attitude toward a product into a positive one. Additionally, when consumers are highly loyal to a brand, they may buy more of that brand when advertising is increased. Last, advertising can also change the importance of a brand's attributes to consumers. By emphasizing different brand attributes, advertisers can change their appeal in response to consumers' changing needs or try to achieve an advantage over competing brands.

1.1 Discuss the reasons why new brands with a smaller market share spend proportionately more on advertising than brands with a larger market share.

TEAM

1.2 Form a three-person team. Divide the responsibility for getting newspaper advertisements and menus for several local restaurants. While you are at the restaurants to obtain copies of their menus, observe the atmosphere and interview the manager to determine what he or she believes are the primary reasons people choose to dine there. Pool your information and develop a table comparing the restaurants in terms of convenience of location, value for the money, food variety and quality, atmosphere, and so on. Rank the restaurants in terms of their appeal to college students. Explain the basis of your rankings. What other market segment would be attracted to the restaurants and why? Do the newspaper advertisements emphasize the most effective appeal for a particular restaurant? Explain.

LO 2

Identify the major types of advertising. Advertising is any form of impersonal, paid communication in which the sponsor or company is identified. The two major types of advertising are institutional advertising and product advertising. Institutional advertising is not product oriented; rather, its purpose is to foster a positive company image among the general public, investment community, customers, and employees. Product advertising is designed mainly to promote goods and services, and it is classified into three main categories: pioneering, competitive, and comparative. A product's place in the product life cycle is a major determinant of the type of advertising used to promote it.

2.1 At what stage in a product's life cycle are pioneering, competitive, and comparative advertising most likely to occur? Give a current example of each type of advertising.

LO3

Discuss the creative decisions in developing an advertising campaign. Before any creative work can begin on an advertising campaign, it is important to determine what goals or objectives the advertising should achieve. The objectives of a specific advertising campaign often depend on the overall corporate objectives and the product being advertised. Once objectives have been defined, creative work can begin on the advertising campaign. Creative decisions include identifying the product's benefits, developing possible advertising appeals, evaluating and selecting the advertising appeals, executing the advertising message, and evaluating the effectiveness of the campaign.

3.1 What is an advertising appeal? Give some examples of advertising appeals you have observed recently in the media.

3.2 Design a full-page magazine advertisement for a new brand of soft drink. The name of the new drink and its package design are at your discretion. On a separate sheet, specify the benefits stressed or appeals made in the advertisement.

LO4

Describe media evaluation and selection techniques. Media evaluation and selection make up a crucial step in the advertising campaign process. Major types of advertising media include newspapers, magazines, radio, television, outdoor advertising such as billboards and bus panels, and the Internet. Recent trends in advertising media include video shopping carts, computer screen savers, cinema and DVD advertising, cell phones, and video games. Promotion managers choose the advertising campaign's media mix on the basis of the following variables: cost per contact, reach, frequency, characteristics of the target audience, flexibility of the medium, noise level, and the life span of the medium. After choosing the media mix, a media schedule designates when the advertisement will appear and the specific vehicles it will appear in.

4.1 What are the advantages of radio advertising? Why is radio expanding as an advertising medium?

4.2 You are the advertising manager of a sailing magazine, and one of your biggest potential advertisers has questioned your rates. Write the firm a letter explaining why you believe your audience selectivity is worth the extra expense for advertisers.

4.3 Identify an appropriate media mix for the following products:

a. Chewing tobacco

b. People magazine

c. Weed-Eaters

d. Foot odor killers

e. "Drink responsibly" campaigns by beer brewers

ONLINE

4.4 How easy is it to find out about advertising options on the Internet? Go to Looksmart's and Yahoo's advertiser pages (**http://www.looksmart.com/aboutus/media** and **http://www.yahoo.com/info/advertising**). What kind of information do they require from you? Send an e-mail requesting information and compare what you receive.

LO5

Discuss the role of public relations in the promotional mix. Public relations is a vital part of a firm's promotional mix. A company fosters good publicity to enhance its image and promote its products. Popular public relations tools include new-product publicity, product placements, consumer education, sponsorships, and Internet Web sites. An equally important aspect of public relations is managing unfavorable publicity to minimize damage to a firm's image.

5.1 How can advertising and publicity work together? Give an example.

5.2 As the new public relations director for a sportswear company, you have been asked to set public relations objectives for a new line of athletic shoes to be introduced to the teen market. Draft a memo outlining the objectives you propose for the shoe's introduction and your reasons for them.

5.3 Review the newspapers in your area for one week. Try to review several and varied newspapers (local, campus, cultural, countercultural, etc.) During this period, cut out all the event advertisements that list sponsors. Once you have your collection, spread them out so you can see them all at once. Identify any patterns or connections between the type of event and its sponsors. Identify companies that sponsor more than one event. What do sponsors tell you about target markets? After analyzing the ads, write a brief paragraph summarizing your discoveries.

Key Terms

advergaming	518
advertising	502
advertising appeal	509
advertising campaign	507
advertising objective	508
advertising response function	503
advocacy advertising	505
audience selectivity	520
cause-related marketing	526
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flighted media schedule	522
frequency	520
infomercial	516
institutional advertising	505
media mix	520
media planning	513
media schedule	522
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public relations	523
pulsing media schedule	522
reach	520
sales promotion	502
seasonal media schedule	522
sponsorship	525
unique selling proposition	509

Exercises

APPLICATION EXERCISE 1

You may think that creating advertising is easy. After all, you have a lot of experience with advertising, having been bombarded with advertisements since you were a child. But creating advertising presents real challenges. In this exercise, you will be challenged to create an ad for a new product for animal use that is based on a product used by humans. Some examples include bras for cows, claw polish for tigers, and "Minute Mice" for cats. You can pick any product and any animal, but the combination must make sense.[80]

Activities

1. You have been hired by the purveyor of your chosen product to create a print advertisement. Lay out your ad on a piece of paper that is no smaller than 8.5 by 11 inches and no larger than 11 by 14 inches. Include a headline, illustration, logo, and body copy. Your illustration may be either hand-drawn or clipped from a magazine.
2. Include the copy for your ad directly on the front of the ad unless your copy blocks are too large for you to be legible or neat. If that is the case, then label your copy blocks with letters, put them on the back of your ad, and write the corresponding letter in the appropriate place on the front of the ad.
3. Don't forget to pick your own brand name for the product or service (like "Minute Mice").

APPLICATION EXERCISE 2

In this age of 24-hour cable news channels, tabloid news shows, and aggressive local and national news reporters intent on exposing corporate wrongdoing, one of the most important skills for a manager to learn is how to deal effectively with the press. Test your ability to deal effectively with the press by putting yourself in the following situation. To make the situation more realistic read the scenario and then give yourself two minutes to write a response to each question.[81]

Activity

Today, in the nation's capital, a public-interest group held a press conference to release the results of a study that found that the food sold in most Chinese restaurants is high in fat. The group claims that the most popular Chinese dishes, including orange chicken, pork fried rice, and Hunan beef, contain nearly as much fat as the food you get from fast-food chains like McDonald's, Wendy's, and Burger King. (Much of it is fried or is covered with heavy sauces.) Furthermore, the group says that customers who hope to keep their cholesterol and blood pressure low by eating Chinese food are just fooling themselves.

A TV reporter from Channel 5 called you at Szechuan Palace, your Szechuan-style Chinese restaurant, to get your response to this study. When he and the camera crew arrived, he asked you the following questions:

1. "A new study released today claims that food sold in Chinese restaurants is on average nearly as fattening as that sold at fast-food restaurants. How healthy is the food that you serve at Szechuan?"
2. "Get the camera in close here [camera closes in to get the shot] because I want the audience at home to see that you don't provide any information on your menu about calories, calories from fat, or cholesterol. Without this information [camera pulls back to get a picture of you and the reporter], how can your customers know whether the food that you serve is healthy for them?"
3. "These new studies were based on lunches and dinners sampled from Chinese restaurants across the nation. A local company, Huntington Labs, has agreed to test foods from local restaurants so that we can provide accurate information to our viewers. Would you agree to let us sample the main dishes in your restaurant to test the level of calories, calories from fat, and cholesterol? Furthermore, can we take the cameras into your restaurant so that we can get your customers' reactions to these studies?"

ETHICS

ETHICS EXERCISE

Creative Advertising Agency has been asked to help its largest client improve its corporate image after a highly publicized product recall. The client requests a television advertisement highlighting the company's generous donation of products to low-income families. The only such donation the company has made, however, is a donation of the recalled products. The account executive fears promoting the donation could cause further consumer backlash, but the client continues to press for the spot.

Questions

1. Should Creative Advertising meet the client's expectations (i.e., create the promotional spot) or risk losing the account? Explain your reasoning.
2. What does the AMA Statement of Ethics say about truth in advertising? Go to **http://www.marketingpower.com** and review the code. Then, write a brief paragraph describing how the AMA Statement of Ethics relates to this issue.

PR NEWSFOTO/© MYSPACE, INC.

Case Study: Myspace

RACY PLACE MYSPACE MAKES BIG-TIME ADVERTISERS WARY

Suddenly, on the Internet, it's 1999. But instead of Hotmail, Yahoo! or ICQ, it's social networking site MySpace.com that is attracting Web surfers at a blistering pace. More than 180,000 visitors are registering every day at a Web site that attracted its first 60 million registered users in under 30 months. Already laying claim to about half the reach that monster players Yahoo! and Google enjoy, MySpace typically draws over 20 million unique visitors each month. And, by the time you read this, all of these statistics will probably have been surpassed, given the site's incomprehensible growth rate.

As Internet success stories go, the MySpace phenomenon is nothing short of spectacular. Rupert Murdoch's News, Inc., bought the site from parent company Intermix Media in 2005 for $580 million, but many observers think that was about one-fourth of what the site could have sold for had the board and the lead investors not rushed into the deal. What reminds industry observers of 1999, though, is that MySpace is a hot property, yet it has no visible business model beyond trading eyeballs for ad dollars.

So why aren't mega advertising dollars flooding the doors at corporate headquarters? A quick tour of MySpace.com would probably answer that question for anyone with a brain and a pulse. MySpace is an anything-goes, youth-oriented, social hub at the center of music, matchmaking, and social rendezvousing. Friends keep in touch with each other by posting their profiles, photos, music preferences, social events, and more to personalized Web pages. The pages they create can host automatically loaded music videos or tracks that start to play as soon as the Web page loads. Pictures are uncensored, as are avatars and messages posted to pages by friends or any registered visitor who happens to land there.

The only thing the site monitors is hate speech, but that may change in the wake of a 2005 controversy in which two sexual predators were convicted of luring minors into sex acts by trolling MySpace's public pages. Skin, lewd language, and descriptions of adult events and activities can be found whenever users care to share or search for them. Not all of the content on MySpace is mature or off-color, however. More than 350,000 music groups or individual performers are registered there, and mainstream acts post pages there so that fans can follow their activities. The Foo Fighters even allowed their album In Your Honor to air free for a week on MySpace before its official release.

The site also hosts hundreds of thousands, possibly millions, of unique video clips in 16 categories. There are blog listings, independent and user-generated film reviews, event listings, classifieds, discussion forums, and, of course, those personal pages and music samples. At least 45 percent of MySpace users are in advertisers' coveted under-25 age bracket. The minimum age requirement is 14, and therein lies the advertisers' rub. Advertising on MySpace raises ethical concerns and sparks fear of unwanted brand association, even though the user base is the most valued.

Though the site claims to generate tens of millions of dollars in ad revenue each month, that pales in comparison to what it could be making. David Cohen, the senior vice president of Interpublic Group's top ad agency, Universal McCann, considers the advertising opportunities on MySpace "a double-edged sword." He points out that user-generated content can be "risqué, in bad taste, et cetera." His Fortune 100 clients don't like the idea of placing advertisements for their products in an environment where they have little control over what appears beside them.

Still, MySpace has its supporters. As the fifth largest Web property on the Internet, it is always going to be attractive to somebody. HSBC, Cingular, Aquafina, and H&R Block have all bought ad space there; surely, many more deep-pocketed firms will follow. As Richard Doherty, research director of Envisioneering Group, asks, "If you pull away from MySpace, where do you go? Do you do due diligence on the next 10 [social networking sites]? Advertisers need this audience. This is a new double-digits-minutes eyeball magnet and advertisers have to be there."[82]

Questions

1. Considering the effects of advertising on consumers, what are the risks that advertisers take in placing advertisements on MySpace?
2. What kind of people or personalities might companies try to appeal to by advertising on MySpace?
3. Do you think the MySpace environment will make it easier or more difficult for advertisers to induce ad viewers to follow the AIDA plan?
4. Compose a list of the companies, products, and services that you think would benefit from advertising on MySpace.com. Are there any in particular that you think should stay away from MySpace, regardless of its popularity?

Company Clips

VANS – OFF THE WALL AND ON MESSAGE

Even though Vans generates $500 million a year in sales, the company uses only a small team to manage the company's advertising and public relations – Stacy and Chris. The Vans PR team (or duo) uses vertical advertising to cater to a core group of consumers. With only a small advertising budget, the team must develop partnerships with its advertisers and use tours and events to spread the Vans culture.

Questions

1. Who does Vans consider to be its core consumers? How does the company reach them with its marketing messages?
2. How does Vans choose causes for its cause-related marketing?
3. What does Vans do to ensure that its print ads fit the publications in which they appear?
4. Describe the role of the Internet in Vans's communication strategy.

Marketing & You Results

High scores indicate that you like television advertising. Not only do you like it, you think television ads have informational benefits. Low scores correspond to a more skeptical attitude toward television advertising. If you are skeptical about television ads, are you also skeptical about print ads and other forms of advertising? How much do you tune out (or tune in)?

ANATOMY OF AN **Advertisement**

Yoplait

1 Media type: Magazine

2 Good color reproduction = Advantage of magazine

3 Advertising appeal = Health, charity

4 Cause-related marketing

5 Long life span: Campaign still running in 2008

6 Product advertising

7 Executional style = Mood

Lamb Hair McDaniel

Marketing

e

Sales Promotion and Personal Selling

CHAPTER

18

Learning Outcomes

LO 1 Define and state the objectives of sales promotion

LO 2 Discuss the most common forms of consumer sales promotion

LO 3 List the most common forms of trade sales promotion

LO 4 Describe personal selling

LO 5 Discuss the key differences between relationship selling and traditional selling

LO 6 List the steps in the selling process

LO 7 Describe the functions of sales management

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LO 1
Sales Promotion

In addition to using advertising, public relations, and personal selling, marketing managers can use sales promotion to increase the effectiveness of their promotional efforts. *Sales promotion* is marketing communication activities, other than advertising, personal selling, and public relations, in which a short-term incentive motivates consumers or members of the distribution channel to purchase a good or service immediately, either by lowering the price or by adding value.

Advertising offers the consumer a reason to buy; sales promotion offers an incentive to buy. Both are important, but sales promotion is usually cheaper than advertising and easier to measure. A major national TV advertising campaign often costs over $5 million to create, produce, and place. In contrast, promotional campaigns using the Internet or direct marketing methods can cost less than half that amount. It is also very difficult to determine how many people buy a product or service as a result of radio or TV ads. But with sales promotion, marketers know the precise number of coupons redeemed or the number of contest entries.

Sales promotion is usually targeted toward either of two distinctly different markets. Consumer sales promotion is targeted to the ultimate consumer market. Trade sales promotion is directed to members of the marketing channel, such as wholesalers and retailers. Sales promotion has become an important element in a marketer's integrated marketing communications program (see Chapter 16). Sales promotion expenditures have been steadily increasing over the last several years as a result of increased competition, the ever-expanding array of available media choices, consumers and retailers demanding more deals from manufacturers, and the continued reliance on accountable and measurable marketing strategies. In addition, product and service marketers that have traditionally ignored sales promotion activities, such as power companies and restaurants, have discovered the marketing power of sales promotion. In fact, annual expenditures on promotion marketing in the United States now exceed $400 billion. Direct mail is the most widely used promotion medium, accounting for almost 50 percent of annual promotion expenditures. The next two most widely used mediums are sampling and in-store promotions. Examples of these include point-of purchase promotions (17 percent of expenditures), events and sponsorships (14 percent), and promotions via Internet and mobile devices (7 percent).[1]

consumer sales promotion Sales promotion activities targeting the ultimate consumer.

trade sales promotion Sales promotion activities targeting a channel member, such as a wholesaler or retailer.

Marketing & You

What do you think of coupons? Enter your answers on the lines provided.

1	2	3	4	5
Strongly disagree				Strongly agree

— Coupons can save a person a lot of money.

— The money I can save by using coupons does not amount to much.*

— I believe that people can help their families financially by using coupons.

— Overall, I like using coupons.

— Personally for me, using coupons for supermarket products is or would be useless.*

— Taking everything into account, using coupons for supermarket shopping is wise.

Now, total your score, reversing your answers for the items followed by an asterisk (for example, if you answered 4, change it to 2). Find out what your score means after you read the chapter.

THE OBJECTIVES OF SALES PROMOTION

Sales promotion usually has more effect on behavior than on attitudes. Immediate

Exhibit 18.1

Types of Consumers and Sales Promotion Goals

Type of Buyer	Desired Results	Sales Promotion Examples
Loyal customers People who buy your product most or all of the time	Reinforce behavior, increase consumption, change purchase timing	• Loyalty marketing programs, such as frequent buyer cards or frequent shopper clubs • Bonus packs that give loyal consumers an incentive to stock up or premiums offered in return for proofs of purchase
Competitor's customers People who buy a competitor's product most or all of the time	Break loyalty, persuade to switch to your brand	• Sampling to introduce your product's superior qualities compared to their brand • Sweepstakes, contests, or premiums that create interest in the product
Brand switchers People who buy a variety of products in the category	Persuade to buy your brand more often	• Any promotion that lowers the price of the product, such as coupons, price-off packages, and bonus packs • Trade deals that help make the product more readily available than competing products
Price buyers People who consistently buy the least expensive brand	Appeal with low prices or supply added value that makes price less important	• Coupons, price-off packages, refunds, or trade deals that reduce the price of the brand to match that of the brand that would have been purchased

SOURCE: From *Sales Promotion Essentials,* 2nd ed., by Don E. Schultz, William A. Robinson, and Lisa A. Petrison. Reprinted by permission of NTC Publishing Group, 4255 Touhy Ave., Lincolnwood, IL 60048.

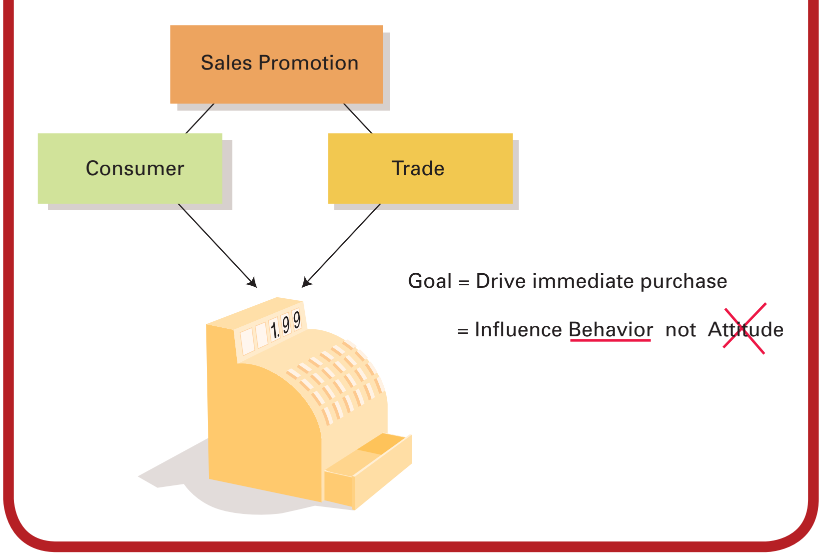
purchase is the goals of sales promotion, regardless of the form it takes. Therefore, it seems to make more sense when planning a sales promotion campaign to target customers according to their general behavior. For instance, is the consumer loyal to your product or to your competitor's? Does the consumer switch brands readily in favor of the best deal? Does the consumer buy only the least expensive product, no matter what? Does the consumer buy any products in your category at all?

The objectives of a promotion depend on the general behavior of target consumers (see Exhibit 18.1). For example, marketers who are targeting loyal users of their product actually don't want to change behavior. Instead, they need to reinforce existing behavior or increase product usage. An effective tool for strengthening brand loyalty is the *frequent buyer program* that rewards consumers for repeat purchases. Other types of promotions are more effective with customers prone to brand switching or with those who are loyal to a competitor's product. A cents-off coupon, free sample, or eye-catching display in a store will often entice shoppers to try a different brand. Consumers who do not use the product may be enticed to try it through the distribution of free samples.

Once marketers understand the dynamics occurring within their product category and have determined the particular consumers and consumer behaviors they want to influence, they can then go about selecting promotional tools to achieve these goals.

REVIEW LEARNING OUTCOME

LO 1 Define and state the objectives of sales promotion



LO 2
Tools for Consumer Sales Promotion

Marketing managers must decide which consumer sales promotion devices to use in a specific campaign. The methods chosen must suit the objectives to ensure success of the overall promotion plan. Popular tools for consumer sales promotion are coupons and rebates, premiums, loyalty marketing programs, contests and sweepstakes, sampling, and point-of-purchase promotion. Consumer sales promotion tools have also been easily transferred to online versions to entice Internet users to visit sites, purchase products, or use services on the Web.

COUPONS AND REBATES

coupon
A certificate that entitles consumers to an immediate price reduction when they buy the product.

A **coupon** is a certificate that entitles consumers to an immediate price reduction when they buy the product. Coupons are a particularly good way to encourage product trial and repurchase. They are also likely to increase the amount of a product bought.

Traditional types of coupon distribution, such as newspapers, direct mail, and magazines, have been declining in the U.S. in recent years, but still represent almost $280 million annually. In contrast, online and in-store distribution of coupons has been increasing. These trends are the result of intense competition in the consumer packaged goods category and the introduction of over 1,200 new products each year. Though coupons are often criticized for reaching customers who have no interest in the product or service, or for encouraging repeat purchase by regular users, studies indicate coupons promote new-product use and are likely to stimulate purchases. The use of colorful Free-standing Inserts (FSI's), mostly in Sunday newspapers, continues to grow despite declines in newspaper readership. But online coupon distribution sites like coolsavings.com and valpak.com are emerging as major coupon distribution outlets. Unfortunately, redemption rates for coupons often are 2 percent or lower.[2]

PR NEWSFOTO/© VALPAK

To overcome the low redemption rates for coupons, marketers are using new strategies. For example, by shortening the time in which coupons can be redeemed or reducing the requirement for multiple purchases, some marketers have increased the redemption rate by creating a greater sense of urgency to redeem the coupon. Some marketers are de-emphasizing their use of coupons in favor of everyday low pricing, while others are distributing single, all-purpose coupons that can be redeemed for several brands.

In-store coupons have become popular because they are more likely to influence customers' buying decisions. Instant coupons on product packages, coupons distributed from on-shelf coupon-dispensing machines, and electronic coupons issued at the check-out counter are achieving much higher redemption rates. Indeed, instant coupons are redeemed more than 15 times more frequently than traditional newspaper coupons, indicating that consumers are making more in-store purchase decisions.

Starbucks has taken in-store coupons to a new level by installing interactive units on grocery store shelves. Each unit provides consumers with product information related to brewing, coffee education, and a taste matcher. In one test the units resulted in a 200 percent increase in sales. Internet coupons are also gaining in popularity. For example, Kroger has launched "Coupons that you click. Not clip." on Kroger.com. Registered Kroger Plus Shoppers card members just log on to the Web site and click on the coupons they want. Coupons are automatically loaded on to the Kroger Plus card and redeemed at checkout when the shopper's Kroger Plus card is scanned.[3]

As marketing tactics grow more sophisticated, coupons are no longer viewed as a stand-alone tactic, but as an integral component of a larger promotional campaign. For example, Domino's Pizza teamed with eBay to launch a "Back to School" campaign focused on building the Domino's brand and driving consumers to **http://www.ebay.com.** The coupons arrived on pizza boxes. Customers then logged on to eBay for a chance to win one million eBay points (a cash value of $10,000) to be spent on eBay.com, textbook discounts, and Domino's gift certificates.[4]

rebate
A cash refund given for the purchase of a product during a specific period.

premium
An extra item offered to the consumer, usually in exchange for some proof of purchase of the promoted product.

loyalty marketing program
A promotional program designed to build long-term, mutually beneficial relationships between a company and its key customers.

frequent buyer program
A loyalty program in which loyal consumers are rewarded for making multiple purchases of a particular good or service.

Rebates are similar to coupons in that they offer the purchaser a price reduction; however, because the purchaser must mail in a rebate form and usually some proof of purchase, the reward is not as immediate. Traditionally used by food and cigarette manufacturers, rebates now appear on all types of products, from computers and software to film and cell phones. In the run-up to Super Bowl XL, Pepsi-Cola offered consumers a $10 dollar rebate as an incentive to stock up on the company's soda products and Frito-Lay brand chips in time for the big game.[5]

Manufacturers prefer rebates for several reasons. Rebates allow manufacturers to offer price cuts to consumers directly. Manufacturers have more control over rebate promotions because they can be rolled out and shut off quickly. Further, because buyers must fill out forms with their names, addresses, and other data, manufacturers use rebate programs to build customer databases. Perhaps the best reason of all to offer rebates is that although rebates are particularly good at enticing purchase, most consumers never bother to redeem them. Studies show only about one-half of customers eligible for rebates actually collect them.[6]

PREMIUMS

A premium is an extra item offered to the consumer, usually in exchange for some proof that the promoted product has been purchased. Premiums reinforce the consumer's purchase decision, increase consumption, and persuade nonusers to switch brands. Premiums like telephones, tote bags, and umbrellas are given away when consumers buy cosmetics, magazines, bank services, rental cars, and so on. Probably the best example of the use of premiums is the McDonald's Happy Meal, which rewards children with a small toy. Many companies have been built around furnishing clients with customized premiums. Because of the ubiquity of premiums, especially in trade relationships, it is getting harder to capture someone's attention with a premium. One British company, Novelty Gift Company, is hoping to change that. The company offers quirky gadgets like pink speakers shaped like pigs, a set of three iPod speakers shaped like a tripod, and a computer mouse that looks like a dragster.[7]

Premiums can also include more product for the regular price, such as two-for-the-price-of-one bonus packs or packages that include more of the product. Kellogg's, for instance, added two more pastries and waffles to its Pop Tarts and Eggo packages without increasing the price in an effort to boost market share lost to private-label brands and new competitors. The promotion was so successful the company decided to keep the additional product in its regular packaging. Another possibility is to attach a premium to the product's package. For example, when research showed that consumers who drink tequila are often trendsetters who entertain at home, 1800 Tequila launched a holiday promotion that included an instant camera and entertainment guide attached to the bottle.[8]

LOYALTY MARKETING PROGRAMS

Loyalty marketing programs, or frequent buyer programs, reward loyal consumers for making multiple purchases. Popularized by the airline industry through frequent flyer programs, loyalty marketing enables companies to strategically invest sales promotion dollars in activities designed to capture greater profits from customers already loyal to the product or company. This is critical, as studies show that consumer loyalty is on the decline. Forrester Research found that the percentage of consumers ranking price as more important than brand rose from 41 to 47 percent over three years. According to research conducted by Gartner, more than 75 percent of consumers have more than one loyalty card that rewards them with redeemable points. Furthermore, there are almost 1.5 billion loyalty program memberships in the U.S., with the average household participating in 12 programs.[9]

The objective of loyalty marketing programs is to build long-term, mutually beneficial relationships between a company and its key customers. Frequent shopper card programs offered by many supermarkets and other retailers have exploded in popularity. Research from Forrester shows that 54 percent of primary grocery shoppers belong to two or more supermarket loyalty programs. Although this speaks to the popularity of loyalty cards, it also shows that customers are pledging "loyalty" to more than one store: 15 percent of primary grocery shoppers are cardholders in at least three programs, and 4 percent participate in four or five programs.[10] Combined with the statistics on the growing importance of price over brands, frequent shopper programs need to offer something more than just discounts to build customer loyalty. One of the more successful recent premium promotions is Starbucks' Duetto Card, which combines a Visa credit card with a reloadable Starbucks card. The card allows members to collect "Duetto Dollars" that can be redeemed for anything they want to purchase at a Starbucks location. Starbucks also sends members quarterly opportunities based on usage, such as product samples and previews. One study reported that over 60 percent of Duetto cardholders said they were more likely to purchase Starbucks products as a result of the program.[11]

Cobranded credit cards are an increasingly popular loyalty marketing tool. Annually over 6 billion direct marketing appeals for a cobranded credit card are sent to potential customers in the United States. Target, Gap, Sony and American Airlines are only a few examples of companies sponsoring cobranded Visa, MasterCard, or American Express cards. American Express has a program with Space Adventures, a company that offers simulated space flight experiences.[12]

Through loyalty programs, shoppers receive discounts, alerts on new products, and other enticing offers. In exchange, retailers are able to build customer databases that help them better understand customer preferences. Verizon Wireless builds loyalty with its "New Every Two" program. Consumers who have been Verizon customers for two years are eligible for a $100 credit toward a new digital phone.[13]

Companies increasingly are using the Internet to build customer loyalty through e-mail and blogs. Over 80 percent of supermarket chains are using e-mail to register customers for their loyalty programs and to entice them with coupons, flyers, and promotional campaigns.[14] Blogs are becoming a critical component of some companies' loyalty marketing programs. Blogging technology enables marketers to create a community of consumers who feel positively about the company's brand and to build deeper relationships with them. Starwood Hotels launched its corporate blog, TheLobby.com, in 2006. Although the blog is open to the public, the company is aiming the content specifically at members of the Starwood Preferred Guest loyalty program. Features include postings about special events at specific Starwood properties and how travelers can earn loyalty points through special promotions. The company's goal is to combine advertising with useful information to create a Web destination for its guests—and divert them away from other travel blogs that might contain negative postings about Starwood hotels.[15]

Companies like McDonald's and Cannondale are also using blogging technology to create communities around their brands. Robin Hopper, CEO of iUpload, the company that hosts the blogs for these two companies, says that companies publish blogs to build social networks around their brands. "It's a whole new way to market," he says. "People willingly provide all sorts of demographic information on blogs" that companies can use to target them more effectively.[16]

CONTESTS AND SWEEPSTAKES

Contests and sweepstakes are generally designed to create interest in a good or service, often to encourage brand switching. *Contests* are promotions in which participants use some skill or ability to compete for prizes. A consumer contest usually requires entrants to answer questions, complete sentences, or write a paragraph about the product and submit proof of purchase. Winning a *sweepstakes*, on the other hand, depends on chance or luck, and participation is free. Sweepstakes usually draw about ten times more entries than contests do.

While contests and sweepstakes may draw considerable interest and publicity, generally they are not effective tools for generating long-term sales. To increase their effectiveness, sales promotion managers must make certain the award will appeal to the target market. For example, Home & Garden Television Network's annual "Dream Home Giveaway" sweepstakes awards a fully furnished, custom-built home to one lucky viewer. The promotion is cosponsored by General Motors, which fills the garage with a new sport-utility vehicle, and other home-related companies such as Sherwin-Williams paint, Lumber Liquidators flooring, California Closets, and Jeld-Wen windows and doors. The annual sweepstakes typically draws over four million entries.[17] Offering several smaller prizes to many winners instead of one huge prize to just one person often will increase the effectiveness of the promotion, but there's no denying the attractiveness of a jackpot-type prize.

PR NEWSFOTO/© KOHL'S DEPARTMENT STORES

Kohl's Department Stores is partnering with Levi's to give away 10 custom 'denim' Volkswagen Beetles, as part of the "Take Home a Show Stopper" sweepstakes.

SAMPLING

sampling
A promotional program that allows the consumer the opportunity to try a product or service for free.

Consumers generally perceive a certain amount of risk in trying new products. Many are afraid of trying something they will not like (such as a new food item) or spending too much money and getting little reward. Sampling allows the customer to try a product risk-free. Sampling can increase retail sales by more than 40 percent.[18] It is no surprise, therefore, that product sampling is the dominant in-store marketing method when it comes to influencing consumer purchase decisions.[19]

Sampling can be accomplished by directly mailing the sample to the customer, delivering the sample door-to-door, packaging the sample with another product, or demonstrating or sampling the product at a retail store or service outlet. Coca-Cola partnered with Domino's Pizza to sample its Coca-Cola Zero beverage. Every Domino's customer placing an order got a complimentary 20-ounce bottle of Coca-Cola Zero. To get the word out about a new flavor of ice cream, Ben & Jerry's Homemade deployed hot-air balloons to summer fairs and festivals in key markets and made guerrilla visits to office buildings in 13 cities. More than one million free scoops were served.[20] Similarly, when Masterfoods wanted to increase sales of its Dove "Promises" product line of dark and milk chocolates, it used both print media and sampling. To reach the upscale target market, samples were handed out at high-end hotels, spas, and gourmet cooking shows.[21]


© FREDERIC J. BROWN/AFP/GETTY IMAGES

Distributing samples can often mitigate the risks consumers perceive in trying a new product. As part of its global marketing strategy, Starbucks has aggressively expanded into Asia. A woman in Hong Kong samples a cup of coffee from "Mercury Man," a Starbucks employee who walks around with a pot of coffee on his back.

Sampling at special events is a popular, effective, and high-profile distribution method that permits marketers to piggyback onto fun-based consumer activities—including sporting events, college fests, fairs and festivals, beach events, and chili cook-offs. For example, product sampling during tailgating at college and professional football stadiums allows marketers to reach anywhere from 10,000 to 50,000 consumers in a single afternoon. H.J. Heinz tests products such as new barbecue sauces and ketchups to get immediate feedback about what consumers like and dislike about the products.[22]

Distributing samples to specific location types where consumers regularly meet for a common objective or interest, such as health clubs, churches, or doctors' offices, is one of the most efficient methods of sampling. What better way to get consumers to try a product than to offer a sample exactly when it is needed most? If someone visits a health club regularly, chances are he or she is a good prospect for a health-food product or vitamin supplement. Health club instructors are also handing out body wash, deodorant, and face cloths to sweating participants at the end of class, and, more surprisingly, hot drinks! Dunkin' Donuts used a sampling program in more than 200 health clubs to promote its new Latte Lite drink, a zero percent fat product that gives health-conscious consumers a lighter alternative.[23] Meanwhile, makers of stain removers and hand cleansers are giving away samples in mall food courts and petting zoos. Likewise, pharmaceutical companies offer free samples of new and expensive drugs as a tactic to entice doctors and consumers to become loyal to a product.

POINT-OF-PURCHASE PROMOTION

point-of-purchase display
A promotional display set up at the retailer's location to build traffic, advertise the product, or induce impulse buying.

Point-of-purchase (P-O-P) promotion includes any promotional display set up at the retailer's location to build traffic, advertise the product, or induce impulse buying. Point-of-purchase promotions include shelf "talkers" (signs attached to store shelves), shelf extenders (attachments that extend shelves so products stand out), ads on grocery carts and bags, end-aisle and floor-stand displays, television monitors at supermarket checkout counters, in-store audio messages, and audiovisual displays. One big advantage of P-O-P promotion is that it offers manufacturers a captive audience in retail stores. Another advantage is that between 70 and 80 percent of all retail purchase decisions are made in-store, so P-O-P promotions can be very effective. P-O-P promotions can increase sales by as much as 65 percent. Strategies to increase sales include adding header or riser cards, changing messages on base or case wraps, adding inflatable or mobile displays, and using signs that advertise the brand's sports, movie, or charity tie-in.[24] When Hershey launched its new Swoops, a "chip" version of popular candy bars such as Almond Joy, Reese's, and Hershey Bars, it successfully used in-store displays to stimulate in-store, impulse purchases of the new candy.[25]

ONLINE SALES PROMOTION

Online sales promotions have expanded dramatically in recent years. Marketers are now spending billions of dollars annually on such promotions. Sales promotions online have proved effective and cost-efficient, generating response rates three to five times higher than those of their off-line counterparts. The most effective types of online sales promotions are free merchandise, sweepstakes, free shipping with purchases, and coupons.

Eager to boost traffic, Internet retailers are busy giving away free services or equipment, such as personal computers and travel, to lure consumers not only to their own Web sites but to the Internet in general. Another goal is to add potential customers to their databases. For example, Heineken USA, Inc. launched the "Headline Hoax" online promotional campaign in which consumers (hoaxers) trick a friend (victim). The hoax is a fake headline with a photograph that looks as though it is on the front page of a major Web page such as Maximonline.com, FHM, or The Sporting News. The hoaxer can choose from a selection of pictures and headlines. One photo shows two football players attacking one another and the tackler has one hand inside the other's shirt and another hand pulling on his shorts; the headline reads "[Person's Name] is too touchy at touch football game." Once the victim opens this e-mail, other friends on the hoaxer's list are alerted to the joke. At the start of the campaign, Heineken had only 5,000 e-mail addresses in its database. Within six months, it had collected an additional 95,000 e-mail addresses. The program has been so successful that it has been updated and expanded to the "Heineken Holiday Headline Hoax" and similar programs.[26]

Marketers have discovered that online coupon distribution provides another vehicle for promoting their products. Online coupons often have a redemption rate of more than 20 percent, as much as 10 times higher than for traditional coupons.[27]

REVIEW LEARNING OUTCOME

LO 2 Discuss the most common forms of consumer sales promotion

In fact, nearly 50 percent of consumers who purchase something online use a coupon or discount promotional code. According to CMS, a coupon-management company, over 2.6 billion coupons are redeemed annually representing $331 billion in potential consumer savings. Moreover, almost 142 million U.S. consumers use coupons each year, with substantial usage across ethnic and demographic lines.[28] In addition, e-coupons can help marketers lure new customers. For example, Staples.com jumped from 23rd to 14th among retail Web sites with the most buyers through an e-coupon promotion that offered $25 off on purchases of $75 or more.[29]

Online versions of loyalty programs are also popping up, and although many types of companies have these programs, the most successful are those run by hotel and airline companies.

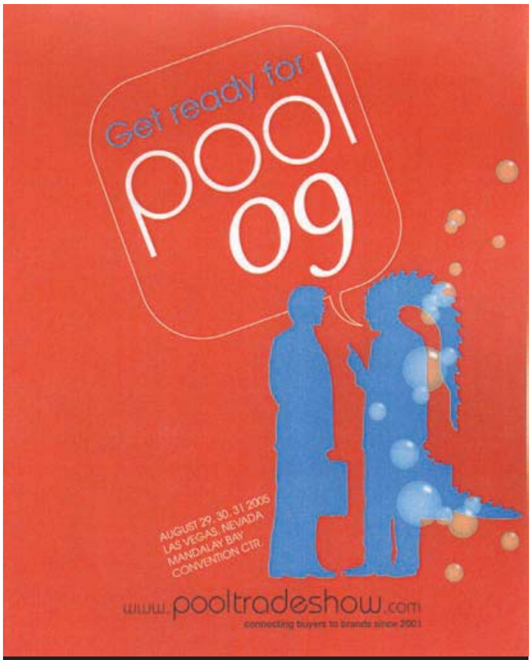
LO 3 Tools for Trade Sales Promotion

Whereas consumer promotions *pull* a product through the channel by creating demand, trade promotions *push* a product through the distribution channel (see Chapter 14). When selling to members of the distribution channel, manufacturers use many of the same sales promotion tools used in consumer promotions—such as sales contests, premiums, and point-of-purchase displays. Several tools, however, are unique to manufacturers and intermediaries:

trade allowance
A price reduction offered by manufacturers to intermediaries, such as wholesalers and retailers.

push money
Money offered to channel intermediaries to encourage them to "push" products—that is, to encourage other members of the channel to sell the products.

- *Trade allowances:* A trade allowance is a price reduction offered by manufacturers to intermediaries such as wholesalers and retailers. The price reduction or rebate is given in exchange for doing something specific, such as allocating space for a new product or buying something during special periods. For example, a local Circuit City or Best Buy outlet could receive a special discount for running its own promotion on Sony Surround Sound Systems.
- *Push money:* Intermediaries receive push money as a bonus for pushing the manufacturer's brand through the distribution channel. Often the push money is directed toward a retailer's salespeople. LinoColor, the leading high-end scanner company, produces a Picture Perfect Rewards catalog filled with merchandise retailers can purchase with points accrued for every LinoColor scanner they sell. The cover of the catalog features a wave runner that was brought to three industry trade shows and given away in a sweepstakes to one of the dealers who had visited all the product displays and passed a quiz. The program resulted in a 26 percent increase in LinoColor sales, and the manufacturer recruited 32 new dealers to carry the product line.[30]
- *Training:* Sometimes a manufacturer will train an intermediary's personnel if the product is rather complex—as frequently occurs in the computer and telecommunication industries. For example, representatives of a TV manufacturer like



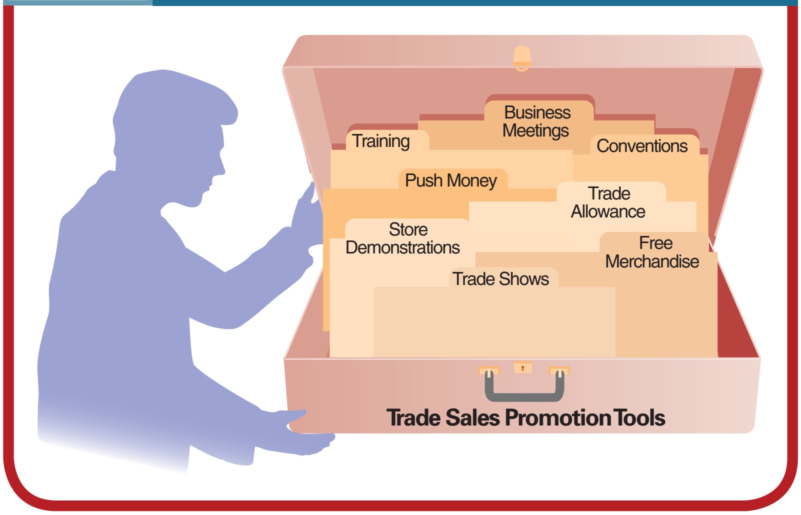
Trade shows and conventions, like the one advertised here, are an increasingly important part of sales promotion; they are an effective way to introduce new products to the marketplace.

Toshiba may train salespeople in how to demonstrate the new features of the latest models of TVs to consumers. This is particularly helpful when salespeople must explain the features to older consumers who are less technology oriented.

- *Free merchandise:* Often a manufacturer offers retailers free merchandise in lieu of quantity discounts. For example, a breakfast cereal manufacturer may throw in one case of free cereal for every 20 cases ordered by the retailer. Occasionally, free merchandise is used as payment for trade allowances normally provided through other sales promotions. Instead of giving a retailer a price reduction for buying a certain quantity of merchandise, the manufacturer may throw in extra merchandise "free" (that is, at a cost that would equal the price reduction).
- *Store demonstrations:* Manufacturers can also arrange with retailers to perform an in-store demonstration. Food manufacturers often send representatives to grocery stores and supermarkets to let customers sample a product while shopping. Cosmetic companies also send their representatives to department stores to promote their beauty aids by performing facials and makeovers for customers.
- *Business meetings, conventions, and trade shows:* Trade association meetings, conferences, and conventions are an important aspect of sales promotion and a growing, multibillion-dollar market. At these shows, manufacturers, distributors, and other vendors have the chance to display their goods or describe their services to customers and potential customers. Moreover, the cost of closing leads generated at trade shows is often less than 50 percent of those developed in the field.[31] Trade shows have been uniquely effective in introducing new products; they can establish products in the marketplace more quickly than advertising, direct marketing, or sales calls can. Companies participate in trade shows to attract and identify new prospects, serve current customers, introduce new products, enhance corporate image, test the market response to new products, enhance corporate morale, and gather competitive product information.

REVIEW LEARNING OUTCOME

LO 3 List the most common forms of trade sales promotion



Trade promotions are popular among manufacturers for many reasons. Trade sales promotion tools help manufacturers gain new distributors for their products, obtain wholesaler and retailer support for consumer sales promotions, build or reduce dealer inventories, and improve trade relations. Car manufacturers annually sponsor dozens of auto shows for consumers. Many of the displays feature interactive computer stations where consumers enter vehicle specifications and get a printout of prices and local dealer names. In return, the local car dealers get the names of good prospects. The shows attract millions of consumers, providing dealers with increased store traffic as well as good leads.

LO4
Personal Selling

personal selling
A purchase situation involving a personal, paid-for communication between two people in an attempt to influence each other.

As mentioned in Chapter 16, personal selling is direct communication between a sales representative and one or more prospective buyers in an attempt to influence each other in a purchase situation.

In a sense, all businesspeople are sales people. An individual may become a plant manager, a chemist, an engineer, or a member of any profession and yet still have to sell. During a job search, applicants must "sell" themselves to prospective employers in an interview. To reach the top in most organizations, individuals need to sell ideas to peers, superiors, and subordinates. Most important, people must sell themselves and their ideas to just about everyone with whom they have a continuing relationship and to many other people they see only once or twice. Chances are that students majoring in business or marketing will start their professional careers in sales. Even students in non-business majors may pursue a sales career.

Personal selling offers several advantages over other forms of promotion:

- Personal selling provides a detailed explanation or demonstration of the product. This capability is especially needed for complex or new goods and services.
- The sales message can be varied according to the motivations and interests of each prospective customer. Moreover, when the prospect has questions or raises objections, the salesperson is there to provide explanations. In contrast, advertising and sales promotion can only respond to the objections the copywriter thinks are important to customers.
- Personal selling can be directed only to qualified prospects. Other forms of promotion include some unavoidable waste because many people in the audience are not prospective customers.
- Personal selling costs can be controlled by adjusting the size of the sales force (and resulting expenses) in one-person increments. On the other hand, advertising and sales promotion must often be purchased in fairly large amounts.
- Perhaps the most important advantage is that personal selling is considerably more effective than other forms of promotion in obtaining a sale and gaining a satisfied customer.

Personal selling may work better than other forms of promotion given certain customer and product characteristics. Generally speaking, personal selling becomes more important as the number of potential customers decreases, as the complexity of the product increases, and as the value of the product grows (see Exhibit 18.2). When there are relatively few potential customers and the value of the good or service is relatively high, the time and travel costs of personally visiting each prospect are justifiable. For highly complex goods, such as business jets or private communication systems, a salesperson is needed to determine the prospective customer's needs, explain the product's basic advantages, and propose the exact features and accessories that will meet the client's needs.

Exhibit 18.2

Comparison of Personal Selling and Advertising/Sales Promotion

Personal selling is more important if . . .	Advertising and sales promotion are more important if . . .
The product has a high value.	The product has a low value.
It is a custom-made product.	It is a standardized product.
There are few customers.	There are many customers.
The product is technically complex.	The product is easy to understand.
Customers are concentrated.	Customers are geographically dispersed.
Examples: insurance policies, custom windows, airplane engines	**Examples:** soap, magazine subscriptions, cotton T-shirts

REVIEW LEARNING OUTCOME

LO4 Describe personal selling

- ✓ Detailed explanation or demonstration
- ✓ Variable sales message
- ✓ Directed at qualified prospects
- ✓ Controllable adjustable selling costs
- ✓ Effective at obtaining sale and gaining customer satisfaction

LO5 Relationship Selling

Until recently, marketing theory and practice concerning personal selling focused almost entirely on a planned presentation to prospective customers for the sole purpose of making the sale. In contrast, modern views of personal selling emphasize the relationship that develops between a salesperson and a buyer. **Relationship selling**, or **consultative selling**, is a multistage process that emphasizes personalization and empathy as key ingredients in identifying prospects and developing them as long-term, satisfied customers. The old way was to sell a product, but with relationship selling, the objective is to build long-term branded relationships with consumers/buyers. Thus, the focus is on building mutual trust between the buyer and seller through the delivery of anticipated, long-term, value-added benefits to the buyer.

relationship selling (consultative selling)
A sales practice that involves building, maintaining, and enhancing interactions with customers in order to develop long-term satisfaction through mutually beneficial partnerships.

Relationship or consultative salespeople, therefore, become consultants, partners, and problem solvers for their customers. They strive to build long-term relationships with key accounts by developing trust over time. The emphasis shifts from a one-time sale to a long-term relationship in which the salesperson works with the customer to develop solutions for enhancing the customer's bottom line. Moreover, research has shown that positive customer-salesperson relationships contribute to trust, increased customer loyalty, and the intent to continue the relationship with the salesperson.[32] Thus, relationship selling promotes a win-win situation for both buyer and seller.

The end result of relationship selling tends to be loyal customers who purchase from the company time after time. A relationship selling strategy focused on retaining customers costs a company less than constantly prospecting and selling to new customers. Companies that focus on customer retention through high customer service gain 6 percent market share per year, while companies that offer low customer service lose 2 percent market share per year.[33] In fact, it costs businesses six times more to gain a new customer than to retain a current one.[34]

Relationship selling is more typical with selling situations for industrial-type goods, such as heavy machinery or computer systems, and services, such as airlines and insurance, than for consumer goods. For example, Kinko's has built a long-term business relationship with PeopleSoft. The software maker now gives many of its training and educational materials printing jobs to Kinko's—a deal worth close to $5 million in revenues. Kinko's has forged such a close relationship with the company that Kinko's representatives are even invited to sit in on internal planning meetings in PeopleSoft's human resources department at the company's headquarters.

"Webinars" (online seminars lasting about an hour) are a popular way to support relationship selling tasks like lead generation, client support, sales training, and corporate meetings. For example, 3Com, a computer data networking system, held a webinar that was attended by 1,300 executives in 80 countries; the session generated 60 percent of 3Com's five-month lead generation goals. Similarly, SpectraLink, a provider of wireless phone and text messaging systems to Verizon and AT&T, uses webinars to give new-product demonstrations so that channel managers can focus on other tasks. DMReview, a web-based portal on technology, has found webinars to be so successful that it offers them continuously "on demand" on business intelligence and data mining topics. The webinars are cosponsored by major firms in insurance, banking, health care, and related fields. To maximize the opportunities provided by webcasting, marketers are using technology that effectively delivers

Exhibit 18.3

Key Differences between Traditional Selling and Relationship Selling

Traditional Personal Selling	Relationship or Consultative Selling
Sell products (goods and services)	Sell advice, assistance, and counsel
Focus on closing sales	Focus on improving the customer's bottom line
Limited sales planning	Consider sales planning as top priority
Spend most contact time telling customers about product	Spend most contact time attempting to build a problem-solving environment with the customer
Conduct "product-specific" needs assessment	Conduct discovery in the full scope of the customer's operations
"Lone wolf" approach to the account	Team approach to the account
Proposals and presentations based on pricing and product features	Proposals and presentations based on profit impact and strategic benefits to the customer
Sales follow-up is short term, focused on product delivery	Sales follow-up is long term, focused on long-term relationship enhancement

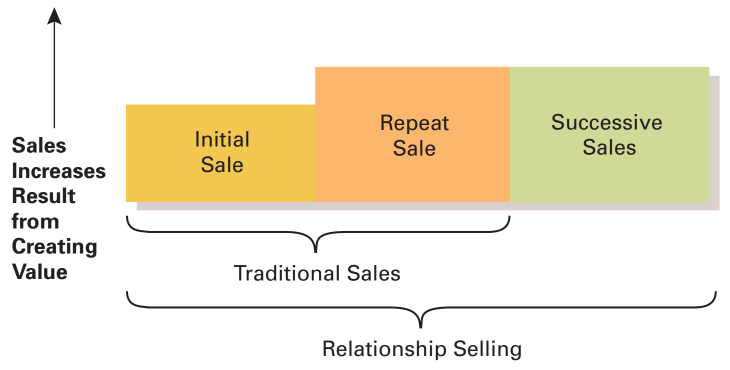
SOURCE: Robert M. Peterson, Patrick L. Schul, and George H. Lucas, Jr., "Consultative Selling: Walking the Walk in the New Selling Environment," National Conference on Sales Management, *Proceedings*, March 1996.

content to other audiences using devices such as mobile phones, TiVo-type digital video recorders, and game consoles.[35]

Exhibit 18.3 lists the key differences between traditional personal selling and relationship or consultative selling. These differences will become more apparent as we explore the personal selling process later in the chapter.

REVIEW LEARNING OUTCOME

LO5 Discuss the key differences between relationship selling and traditional selling



LO6 Steps in the Selling Process

Although personal selling may sound like a relatively simple task, completing a sale actually requires several steps. The **sales process**, or **sales cycle**, is simply the set of steps a salesperson goes through to sell a particular product or service. The sales process or cycle can be unique for each product or service, depending on the features of the product or service, characteristics of customer segments, and internal processes in place within the firm, such as how leads are gathered.

Some sales take only a few minutes, but others may take much longer to complete. Sales of technical products, such as a Boeing or Airbus airplane, and customized goods and services typically take many months, perhaps even years, to complete. On the other end of the spectrum, sales of less technical products like copy machines or office supplies are generally more routine and may take only a few days. Whether a salesperson spends a few minutes or a few years on a sale, these are the seven basic steps in the personal selling process:

1. Generating leads
2. Qualifying leads
3. Approaching the customer and probing needs

sales process (sales cycle) The set of steps a salesperson goes through in a particular organization to sell a particular product or service.

Exhibit 18.4

Relative Amount of Time Spent in Key Steps of the Selling Process

Key Selling Steps	Traditional Selling	Relationship/Consultative Selling
Generating leads	High	Low
Qualifying leads	Low	High
Approaching the customer and probing needs	Low	High
Developing and proposing solutions	Low	High
Handling objections	High	Low
Closing the sale	High	Low
Following up	Low	High

4. Developing and proposing solutions
5. Handling objections
6. Closing the sale
7. Following up

Like other forms of promotion, these steps of selling follow the AIDA concept discussed in Chapter 16. Once a salesperson has located a prospect with the authority to buy, he or she tries to get the prospect's attention. A thorough needs assessment turned into an effective sales proposal and presentation should generate interest. After developing the customer's initial desire (preferably during the presentation of the sales proposal), the salesperson seeks action in the close by trying to get an agreement to buy. Follow-up after the sale, the final step in the selling process, not only lowers cognitive dissonance (refer to Chapter 6) but also may open up opportunities to discuss future sales. Effective follow-up will also lead to repeat business in which the process may start all over again at the needs assessment step.

Traditional selling and relationship selling follow the same basic steps. They differ in the relative importance placed on key steps in the process (see Exhibit 18.4). Traditional selling efforts are transaction oriented, focusing on generating as many leads as possible, making as many presentations as possible, and closing as many sales as possible. Minimal effort is placed on asking questions to identify customer needs and wants or matching these needs and wants to the benefits of the product or service. In contrast, the salesperson practicing relationship selling emphasizes an up-front investment in the time and effort needed to uncover each customer's specific needs and wants and matches the product or service offering to them as closely as possible. By doing the homework up front, the salesperson creates the conditions necessary for a relatively straightforward close. Let's look at each step of the selling process individually.

GENERATING LEADS

lead generation (prospecting) Identification of those firms and people most likely to buy the seller's offerings.

Initial groundwork must precede communication between the potential buyer and the salesperson. Lead generation, or prospecting, is the identification of those firms and people most likely to buy the seller's offerings. These firms or people become "sales leads" or "prospects."

Sales leads can be obtained in several different ways, most notably through advertising, trade shows and conventions, or direct-mail and telemarketing programs. One accounting firm used direct mail, telephone, sales visits, and seminars in a four-step process aimed at generating business-to-business leads. The initial step was a direct-mail piece, in the form of an introductory letter from a firm partner. The second piece, sent one month later, was a black and white direct-mail circular with company contact information. The third step was a follow-up call from a firm partner to arrange a meeting. In the last stage, partners contacted prospects who had initially declined appointments and invited them to attend a free tax seminar the following month. Of the 1,100 businesses targeted, 200 prospects set up meetings. Favorable publicity also helps to create leads. Company records of past client purchases are another excellent source of leads. Many sales professionals are also securing valuable leads from their firm's Internet Web site. For example, Chrysler's use of interactive media to create ongoing interaction with online consumers is paying off. The company recently sponsored 42 online video games featuring Chrysler, Jeep, and Dodge vehicles, generating more than 10,000 sales

referral
A recommendation to a salesperson from a customer or business associate.

networking
A process of finding out about potential clients from friends, business contacts, coworkers, acquaintances, and fellow members in professional and civic organizations.

lead qualification
Determination of a sales prospect's (1) recognized need, (2) buying power, and (3) receptivity and accessibility.

leads among the estimated 3.5 million consumers who downloaded the games. The company generates an estimated 40,000 sales leads monthly through its Web site and other online venues.[36]

Another way to gather a lead is through a referral—a recommendation from a customer or business associate. The advantages of referrals over other forms of prospecting include highly qualified leads, higher closing rates, larger initial transactions, and shorter sales cycles. Simply put, the salesperson and the company can earn more money in less time when prospecting using referrals. Referrals typically are as much as ten times more productive in generating sales than are cold calls. Unfortunately, although most clients are willing to give referrals, many salespeople do not ask for them. Effective sales training can help to overcome this reluctance to ask for referrals. To increase the number of referrals they receive, some companies even pay or send small gifts to customers or suppliers who provide referrals.

Networking is being transformed by the Internet. Sites like LinkedIn connect the contact lists of thousands of users, creating easily navigable networks comprised of millions of people working in nearly every industry.

Networking is using friends, business contacts, coworkers, acquaintances, and fellow members in professional and civic organizations to identify potential clients. Indeed, a number of national networking clubs have been started for the sole purpose of generating leads and providing valuable business advice. The networking clubs usually have between 15 and 30 members in noncompeting business categories. During weekly breakfast or lunch meetings, each member is allowed to talk about the company he or she represents for an allotted period of time. Then members exchange lead cards. Research suggests that, on average, chapter members see an increase in business volume of between 16 and 25 percent after they've been with their group for three to six months. Increasingly, sales professionals are also using online networking sites such as Ryze, LinkedIn, and Zero Degrees to connect with targeted leads and clients around the world, 24 hours a day. Some of LinkedIn's estimated 4.8 million users have reported response rates between 50 and 60 percent, versus 3 percent from direct marketing efforts.[37]

QUALIFYING LEADS

When a prospect shows interest in learning more about a product, the salesperson has the opportunity to follow up, or qualify, the lead. Personally visiting unqualified prospects wastes valuable salesperson time and company resources. Often many leads go unanswered because salespeople are given no indication as to how qualified the leads are in terms of interest and ability to purchase. Unqualified prospects give vague or incomplete answers to a salesperson's specific questions, try to evade questions on budgets, and request changes in standard procedures like prices or terms of sale. In contrast, qualified leads who represent real prospects answer questions, value your time, and are realistic about money and when they are prepared to buy. Salespersons who are given accurate information on qualified leads are more than twice as likely to follow up.[38]

Lead qualification involves determining whether the prospect has three things: a recognized need, willingness to see a salesperson, and buying power. Lead qualification is often handled by a telemarketing group or a sales support person who prequalifies the lead for the salesperson. But companies are increasingly using their Web sites to qualify leads. When leads are qualified online, companies want visitors to register, indicate the products and services they are interested in, and provide information on their time frame and resources. Leads from the Internet can then be prioritized (those indicating a short time frame, for instance, given a higher priority) and then transferred to salespeople. Often Web site visitors can be enticed to answer questions with offers of free merchandise or information. Enticing visitors to register also enables companies to customize future electronic interactions—for example, by giving prospects who visit the Web site their choice from a menu of products tailored specifically to their needs.

APPROACHING THE CUSTOMER AND PROBING NEEDS

preapproach
A process that describes the "homework" that must be done by a salesperson before he or she contacts a prospect.

needs assessment
A determination of the customer's specific needs and wants, and the range of options the customer has for satisfying them.

Before approaching the customer, the salesperson should learn as much as possible about the prospect's organization and its buyers. This process, called the preapproach, describes the "homework" that must be done by the salesperson before contacting the prospect. This may include consulting standard reference sources, such as Moody's, Standard & Poor's, or Dun & Bradstreet, or contacting acquaintances or others who may have information about the prospect. Another preapproach task is to determine whether the actual approach should be a personal visit, a phone call, a letter, or some other form of communication.

During the sales approach, the salesperson either talks to the prospect or secures an appointment for a future time in which to probe the prospect further as to his or her needs. Relationship selling theorists suggest that salespeople should begin developing mutual trust with their prospect during the approach. Salespeople should use the approach as a way of introducing themselves and their company and products. They must sell themselves before they can sell the product. Small talk that projects sincerity and some suggestion of friendship is encouraged because it builds rapport with the prospect, but remarks that could be construed as insincere should be avoided.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The salesperson's ultimate goal during the approach is to conduct a needs assessment to find out as much as possible about the prospect's situation. This involves interviewing the customer to determine his or her specific needs and wants and the range of options the customer has for satisfying them. The salesperson should be determining how to maximize the fit between what he or she can offer and what the prospective customer wants. In conducting a needs assessment, consultative salespeople must learn about the product or service, the customers and their needs, the competition, and the industry. Using this information, a customer profile is created.

Creating a *customer profile* during the approach helps salespeople optimize their time and resources. This profile is then used to help develop an intelligent analysis of the prospect's needs in preparation for the next step, developing and proposing solutions. Customer profile information is typically stored and manipulated using sales force automation software packages designed for use on laptop computers. Sales force automation software provides sales reps with a computerized and efficient method of collecting customer information for use during the entire sales process. Further, customer and sales data stored in a computer database can be easily shared among sales team members. The information can also be appended with industry statistics, sales or meeting notes, billing data, and other information that may be pertinent to the prospect or the prospect's company. The more salespeople know about their prospects, the better they can meet their needs.

DEVELOPING AND PROPOSING SOLUTIONS

Once the salesperson has gathered the appropriate information about the client's needs and wants, the next step is to determine whether his or her company's products or services match the needs of the prospective customer. The salesperson then develops a solution, or possibly several solutions, in which the salesperson's product or service solves the client's problems or meets a specific need.

sales proposal
A formal written document or professional presentation that outlines how the salesperson's product or service will meet or exceed the prospect's needs.

sales presentation
A formal meeting in which the salesperson presents a sales proposal to a prospective buyer.

These solutions are typically offered to the client in the form of a sales proposal delivered during a sales presentation. A sales proposal is a written document or professional presentation that outlines how the company's product or service will meet or exceed the client's needs. The sales presentation is the formal meeting in which the salesperson has the opportunity to present the sales proposal. The presentation should be explicitly tied to the prospect's expressed needs. Further, the prospect should be involved in the presentation by being encouraged to participate in demonstrations or by exposure to computer exercises, slides, video or audio, flipcharts, photographs, and the like.

Technology has become an important part of presenting solutions for many salespeople. Pen manufacturer BIC uses the Internet to connect with its wholesale and convenience store customers. Before launching BIClink.com, BIC received 80 percent of its order volume by fax. Processing these orders was time-consuming, and the orders often were filled with errors. BIClink.com has eliminated the potential for errors and made it easier and faster to validate purchase order numbers, ship dates, case quantities, and pricing. When customers sign on (through a secure, password-protected system), the welcome screen is personalized with their company's name and the name of their BIC rep. On placing an order, customers receive both a hard copy and e-mail confirmation statement with the salesperson's name and contact information including e-mail, voice mail, phone, and fax numbers. Virtually all of BIC's customers now order online.[39]

Because the salesperson often has only one opportunity to present solutions, the quality of both the sales proposal and presentation can make or break the sale. Salespeople must be able to present the proposal and handle any customer objections confidently and professionally. For a powerful presentation, salespeople must be well prepared, use direct eye contact, ask open-ended questions, be poised, use hand gestures and voice inflection, focus on the customer's needs, incorporate visual elements that impart valuable information, know how to operate the audio/visual or computer equipment being used for the presentation, make sure the equipment works, and practice, practice, practice.[40] Nothing dies faster than a boring presentation. If the salesperson doesn't have a convincing and confident manner, then the prospect will very often forget the information. Prospects take in body language, voice patterns, dress, and body type. Often customers are more likely to remember how salespeople present themselves than what they say.

HANDLING OBJECTIONS

Rarely does a prospect say "I'll buy it" right after a presentation. Instead, the prospect often raises objections or asks questions about the proposal and the product. The potential buyer may insist that the price is too high, that he or she does not have enough information to make a decision, or that the good or service will not satisfy the present need. The buyer may also lack confidence in the seller's organization or product.


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One of the first lessons that every salesperson learns is that objections to the product should not be taken personally as confrontations or insults. Rather, a salesperson should view objections as requests for information. A good salesperson considers objections a legitimate part of the purchase decision. To handle objections effectively, the salesperson should anticipate specific objections, such as concerns about price, fully investigate the objection with the customer, be aware of what the competition is offering, and, above all, stay calm. When Dell introduced its direct selling model, salespeople anticipated that customers would worry that they would not receive the same level of service and dedication as they would get from a reseller. As a result, the salespeople included assurances about service and support following the sale in their sales presentations.

Zig Ziglar, a renowned sales trainer, created a popular method for handling objections: "When an objection occurs, always use the fundamentals of FEEL, FELT, FOUND. It gives you an extra cushion of time and allows the prospect to identify with others." For example: "I see how you FEEL! Others have FELT the same way too until they FOUND . . . ." In the Xerox copier example, the doctor might say, "The copy machine seems to be very expensive." Using the Zig Ziglar method the salesperson would respond, "I see how you *feel*. Other doctors have *felt* the same way until they *found* out how much money they were saving after the first year."[41]

Often the salesperson can use the objection to close the sale. If the customer tries to pit suppliers against each other to drive down the price, the salesperson should be prepared to point out weaknesses in the competitor's offer and stand by the quality in his or her own proposal.

CLOSING THE SALE

At the end of the presentation, the salesperson should ask the customer how he or she would like to proceed. If the customer exhibits signs that he or she is ready to purchase and all questions have been answered and objections have been met, then the salesperson can try to close the sale. Customers often give signals during or after the presentation that they are ready to buy or are not interested. Examples include changes in facial expressions, gestures, and questions asked. The salesperson should look for these signals and respond appropriately.

Closing requires courage and skill. Naturally, the salesperson wants to avoid rejection, and asking for a sale carries with it the risk of a negative answer. A salesperson should keep an open mind when asking for the sale and be prepared for either a yes or a no. Rarely is a sale closed on the first call. In fact, the typical salesperson makes several hundred sales calls a year, many of which are repeat calls to the same client in an attempt to make a sale. Some salespeople may negotiate with large accounts for several years before closing a sale. As you can see, building a good relationship with the customer is very important. Often, if the salesperson has developed a strong relationship with the customer, only minimal efforts are needed to close a sale.

negotiation
The process during which both the salesperson and the prospect offer special concessions in an attempt to arrive at a sales agreement.

Negotiation often plays a key role in the closing of the sale. Negotiation is the process during which both the salesperson and the prospect offer special concessions in an attempt to arrive at a sales agreement. For example, the salesperson may offer a price cut, free installation, free service, or a trial order. Effective negotiators, however, avoid using price as a negotiation tool because cutting price directly affects a company's profitability. Because companies spend millions on advertising and product development to create value, when salespeople give in to price negotiations too quickly, it decreases the value of the product. Instead, effective salespeople should emphasize value to the customer, rendering price a nonissue. Salespeople should also be prepared to ask for trade-offs and try to avoid giving unilateral concessions. If you're making only a 50 percent margin on a product, and you need at least a 60 percent margin, raise your prices or drop the product. Moreover, if the customer asks for a 5 percent discount, the salesperson should ask for something in return, such as higher volume or more flexibility in delivery schedules.

FOLLOWING UP

Unfortunately, many salespeople have the attitude that making the sale is all that's important. Once the sale is made, they can forget about their customers. They are wrong. Salespeople's responsibilities do not end with making the sales and placing

follow-up
The final step of the selling process, in which the salesperson ensures that delivery schedules are met, that the goods or services perform as promised, and that the buyers' employees are properly trained to use the products.

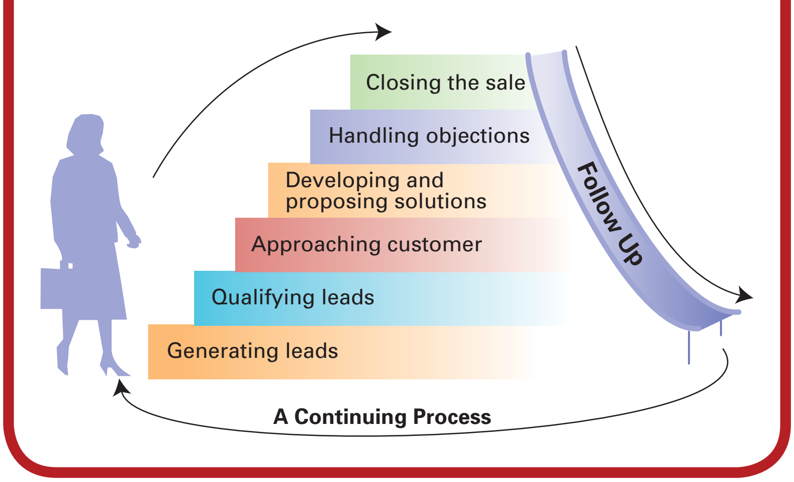
the orders. One of the most important aspects of their jobs is follow-up—the final step in the selling process, in which they must ensure that delivery schedules are met, that the goods or services perform as promised, and that the buyers' employees are properly trained to use the products.

In the traditional sales approach, follow-up with the customer is generally limited to successful product delivery and performance. A basic goal of relationship selling is to motivate customers to come back, again and again, by developing and nurturing long-term relationships. Most businesses depend on repeat sales, and repeat sales depend on thorough and continued follow-up by the salesperson. Finding a new customer is far more expensive than retaining an existing customer. When customers feel abandoned, cognitive dissonance arises and repeat sales decline. Today, this issue is more pertinent than ever because customers are far less loyal to brands and vendors. Buyers are more inclined to look for the best deal, especially in the case of poor after-the-sale follow-up. More and more buyers favor building a relationship with sellers. One Farmers' Insurance agent suggests following up on insurance claims with a question to determine the customer's level of satisfaction. For example, he may ask "Were you happy with the way your claim was handled?" Depending on the response, the agent can either get a referral from the customer or try to fix any problems so that the customer does not choose another agency in the future. This agent also makes telephone and personal follow-up visits after a marriage, death, birth, or birthday in the customer's family. These visits are used as sales opportunities to cross-sell products such as life insurance.[42]

Automated e-mail follow-up marketing—a combination of sales automation and Internet technology—is enhancing customer satisfaction as well as bringing in more business for some marketers. Here's how it works: After the initial contact with a prospect, a software program automatically sends a series of personalized e-mails over a period of time. CollegeRecruiter.com is one company taking advantage of this technology. The company posts ads for businesses recruiting recent college graduates on its Web site and has seen phenomenal results from autoresponse marketing. Prospects start receiving a series of e-mails once they have visited the site and requested advertising rates. The first message goes out immediately. The next two go out in 4 to 11 days. From there, e-mails go out monthly. Using the automated follow-up e-mail system has helped CollegeRecruiter.com become the highest traffic career site used by job-hunting students and recent graduates. Its Web site regularly posts more than 100,000 job openings.[43]

REVIEW LEARNING OUTCOME

LO6 List the steps in the selling process



LO7 Sales Management

There is an old adage in business that nothing happens until a sale is made. Without sales there is no need for accountants, production workers, or even a company president. Sales provide the fuel that keeps the corporate engines humming. Companies like Cisco Systems, International Paper, Johnson Controls, and several thousand other manufacturers would cease to exist without successful salespeople. Even companies like Procter & Gamble and Kraft Foods that mainly sell consumer goods and use extensive advertising campaigns still rely on salespeople to move products through the channel of distribution. Thus, sales management is one of marketing's most critical specialties. Effective sales management stems from a highly success-oriented sales force that accomplishes its mission economically and efficiently. Poor sales management can lead to unmet profit objectives or even to the downfall of the corporation.

Just as selling is a personal relationship, so is sales management. Although the sales manager's basic job is to maximize sales at a reasonable cost while also maximizing profits, he or she also has many other important responsibilities and decisions:

1. Defining sales goals and the sales process
2. Determining the sales force structure
3. Recruiting and training the sales force
4. Compensating and motivating the sales force
5. Evaluating the sales force

DEFINING SALES GOALS AND THE SALES PROCESS

Effective sales management begins with a determination of sales goals. Without goals to achieve, salesperson performance would be mediocre at best, and the company would likely fail. Like any marketing objective, sales goals should be stated in clear, precise, and measurable terms and should always specify a time frame for their fulfillment. Overall sales force goals are usually stated in terms of desired dollar sales volume, market share, or profit level. For example, a life insurance company may have a goal to sell $50 million in life insurance policies annually, to attain a 12 percent market share, or to achieve $1 million in profits. Individual salespeople are also assigned goals in the form of quotas. A quota is simply a statement of the salesperson's sales goals, usually based on sales volume alone but sometimes including key accounts (those with greatest potential), new accounts, repeat sales, and specific products.

quota
A statement of the individual salesperson's sales objectives, usually based on sales volume alone but sometimes including key accounts (those with greatest potential), new accounts, repeat sales, and specific products.

DETERMINING THE SALES FORCE STRUCTURE

Because personal selling is so costly, no sales department can afford to be disorganized. Proper design helps the sales manager organize and delegate sales duties and provide direction for salespeople. Sales departments are most commonly organized by geographic regions, by product line, by marketing function performed (such as account development or account maintenance), by market or industry, or by individual client or account. The sales force for Hewlett-Packard could be organized into sales territories covering New England, the Midwest, the South, and the West Coast or into distinct groups selling different product lines. HP salespeople may also be assigned to a specific industry or market, for example, the telecommunications industry, or to key clients such as AT&T, Cingular, Virgin Mobile, and Verizon.

Market- or industry-based structures and key account structures are gaining popularity in today's competitive selling environment, especially with the emphasis on relationship selling. Being familiar with one industry or market allows sales reps to become experts in their fields and thereby offer better solutions and service. Further, by organizing the sales force around specific customers, many companies hope to improve customer service, encourage collaboration with other arms of the company, and unite salespeople in customer-focused sales teams.

RECRUITING AND TRAINING THE SALES FORCE

Sales force recruitment should be based on an accurate, detailed description of the sales task as defined by the sales manager. For example, General Electric recruits over 1,000 students on 100 college campuses across the United States for entry-level, internship, and co-op positions each year. Its Web site provides prospective salespeople with explanations of different career entry paths and video accounts of what it is like to have a career at GE. Aside from the usual characteristics such as level of experience or education, what traits should sales managers look for in applicants? One of the most important traits of top performers is ego strength, or having a strong, healthy self-esteem and the ability to bounce back from rejection. Great salespeople also have a sense of urgency and competitiveness that pushes their sales to completion. Moreover, they have a desire to persuade people and close the sale. Effective salespeople are also assertive; they have the ability to be firm in one-to-one negotiations, to lead the sales process, and to get their point across confidently, without being overbearing or aggressive. They are sociable, willing to take risks, and capable of understanding complex concepts and ideas. Additionally, great salespeople are creative in developing client solutions, and they possess empathy—the ability to place oneself in someone else's shoes. Not surprisingly, virtually all successful salespeople say their sales style is relationship oriented rather than transaction oriented.[44]

After the sales recruit has been hired and given a brief orientation, training begins. A new salesperson generally receives instruction in company policies and practices, selling techniques, product knowledge, industry and customer characteristics, and nonselling duties such as filling out sales and market information reports or using a sales automation computer program. Firms that sell complex products generally offer the most extensive training programs. Once applicants are hired at General Electric, they enter one of the many "rotational" training programs depending on their interest and major. For example, the Sales and Marketing Commercial Leadership Program (CLP) is geared toward developing skills needed for a successful career at GE. The program ranges from one to two years, depending on which GE business area the employee selects, and includes several rotations between business headquarters and the field. On completing the program, the new employees are better prepared to sell GE products because of their high level of product knowledge and on-the-job experience interacting with customers.[45]

COMPENSATING AND MOTIVATING THE SALES FORCE

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Compensation planning is one of the sales manager's toughest jobs. Only good planning will ensure that compensation attracts, motivates, and retains good salespeople. Generally, companies and industries with lower levels of compensation suffer higher turnover rates, which increase costs and decrease effectiveness. Therefore, compensation needs to be competitive enough to attract and motivate the best salespeople. Firms sometimes take profit into account when developing their compensation plans. Instead of paying salespeople on overall volume, they pay according to the profitability achieved from selling each product. Still other companies tie a part of the salesperson's total compensation to customer satisfaction assessed through periodic customer surveys.

As the emphasis on relationship selling increases, many sales managers feel that tying a portion of a salesperson's compensation to a client's satisfaction with the salesperson and the company encourages relationship building. To determine this, sales managers can survey clients on a salesperson's ability to create realistic expectations and his or her responsiveness to customer needs. At PeopleSoft, the world's second largest applications software company, structure, culture, and strategies are built around customer satisfaction. Sales force compensation is tied to both sales quotas and a satisfaction metric that allows clients to voice their opinions on the service provided.[46]

Although the compensation plan motivates a salesperson to sell, sometimes it is not enough to produce the volume of sales or the profit margin required by sales management. Sales managers, therefore, often offer rewards or incentives, such as recognition at ceremonies, plaques, vacations, merchandise, and pay raises or cash bonuses. For example, Lorry I. Lokey, founder and chairman of the board of Business Wire, has invited employees from one of the company's 26 offices nationwide to join him on a free trip to a predetermined location, usually overseas. To qualify, employees must have celebrated their five-year anniversary with the company.[47] But, of course, cash awards are the most popular sales incentive and are used by virtually all companies. Another possibility is to reward salespeople with a Visa Gift Card, available from Visa in any amount between $25 and $600. The gift card, which functions like a credit card, can be personalized with a message about the salesperson's performance. It can then be reloaded at the employer's discretion. To recognize and further motivate employees, General Electric uses various rewards including stock options, recognition programs unique to each department, tuition assistance, and product discounts.[48] Rewards may help increase overall sales volume, add new accounts, improve morale and goodwill, move slow items, and bolster slow sales. They can also be used to achieve long-term or short-term objectives, such as unloading overstocked inventory and meeting a monthly or quarterly sales goal. In motivating their sales force, sales managers must be careful not to encourage unethical behavior, as the "Ethics in Marketing" box explains.

ETHICS in Marketing

Promoting Ethical Behavior in Business

ETHICS

It is important for all companies to monitor their corporate cultures. This is especially true when salespeople are motivated by sales incentives. Salespeople's behavior often reflects the company's sales management program.

To develop a training program that will produce an ethical and successful sales force, sales managers should consider the company's mission statement, employee incentives, and compensation. When developing or modifying the mission statement, managers and employees should consider their customers' needs and wants. Salespeople who must try to sell unnecessary or unwanted products are more likely to cross ethical boundaries.

Sales managers should also consider what motivates employees to sell the company's product or service. Aside from compensation, many companies offer some type of incentive package, such as a trip, merchandise, or extra vacation time, that is based on the volume or dollars sold. Sales managers must also guard against unintended negative consequences of the incentives they offer.

Compensation policies are a major ethical issue for many sales-motivated organizations and must be designed to discourage unethical behavior.

Finally, sales managers should regularly evaluate and review the performance of their salespeople to make sure that they are not engaging in unethical behavior. In their book *The Psychology of Sales Call Reluctance,* George Dudley and Shannon Goodson include a list labeled "How to Spot Unethical Self-Promoters." It provides a good guide to unethical salesperson behaviors. For example:

1. *Compulsive name-dropping:* Unethical salespeople know everybody you need them to know in order to impress you with their social network, contacts, and connections.
2. *Unshakable:* They are inappropriately calm and poised—even when you catch them in a lie.
3. *Dismissive:* When caught lying and confronted, they explain deception as a "harmless misunderstanding."
4. *Camouflage:* Their air of confidence and superiority conceals a history of legal problems and "misunderstandings."
5. *Fakes sincerity:* They tenaciously project phony sincerity because in their view, "everyone else is doing it."
6. *Mirror:* They repeatedly say whatever is necessary to make you think they acknowledge and closely identify with your values, interests, ambitions, and objectives.
7. *Aggressively advertise personal virtues:* They habitually package self-presentation with words like integrity, openness, trust, principles, and honesty.

Sales managers can use guidelines like these to identify individuals who may be using unethical approaches. By carefully reviewing performance and developing an incentive and compensation program that properly motivates employees, sales mangers can help to ensure that their company has an ethical sales force.[49]

Source: From Kathleen Cholewka, "E-Market Stats", 'Sales & Marketing', September 1, 2001

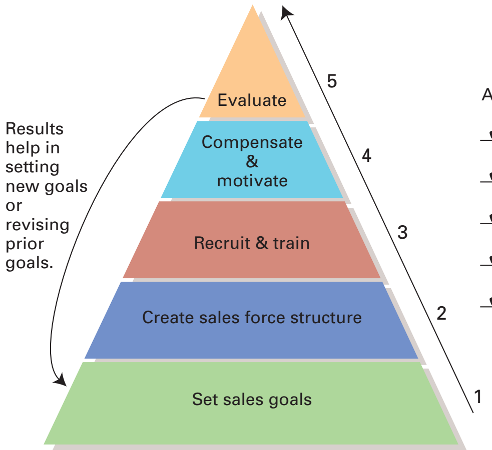
EVALUATING THE SALES FORCE

The final task of sales managers is evaluating the effectiveness and performance of the sales force. To evaluate the sales force, the sales manager needs feedback—that is, regular information from salespeople. Typical performance measures include sales volume, contribution to profit, calls per order, sales or profits per call, or percentage of calls achieving specific goals such as sales of products that the firm is heavily promoting.

Performance information helps the sales manager monitor a salesperson's progress through the sales cycle and pinpoint where breakdowns may be occurring. For example, by learning the number of prospects an individual salesperson has in each step of the sales cycle process and determining where prospects are falling out of the sales cycle, a manager can determine how effective a salesperson may be at lead generation, needs assessment, proposal generation, presenting, closing, and follow-up stages. This information can then tell a manager what sales skills may need to be reassessed or retrained. For example, if a sales manager notices that a sales rep seems to be letting too many prospects slip away after presenting proposals, it may mean he or she needs help with developing proposals, handling objections, or closing sales.

REVIEW LEARNING OUTCOME

LO7 Describe the functions of sales management



As a sales tool, technology can:

- ✓ Ease administration burden
- ✓ Arm salespeople with valuable information
- ✓ Track sales performance individually and company-wide
- ✓ Enable collaboration
- ✓ Make sales management more effective

$5 million < cost of creating, producing, and placing a national TV advertising campaign

new products introduced each year > **1,200**

2 < percentage of coupons that are redeemed

percentage of online coupons that are redeemed > **20**

1.5 billion < loyalty program memberships in the U.S.

health clubs in which Dunkin' Donuts distributed samples of its Latte Lite drink > **200**

6 < percentage of market share gained each by companies with high customer service

2 < percentage of market share lost by companies with low customer service

online video games sponsored by Chrysler and featuring their vehicles > **42**

100,000 < job openings on CollegeRecruiter.com

Review and Applications

LO 1

Define and state the objectives of sales promotion. Sales promotion consists of those marketing communication activities, other than advertising, personal selling, and public relations, in which a short-term incentive motivates consumers or members of the distribution channel to purchase a good or service immediately, either by lowering the price or by adding value. The main objectives of sales promotion are to increase trial purchases, consumer inventories, and repeat purchases. Sales promotion is also used to encourage brand switching and to build brand loyalty. Sales promotion supports advertising activities.

1.1 What is the primary factor that determines sales promotion objectives? Name some different types of sales promotion techniques, and explain the type of customer they are intended to influence.

WRITING

1.2 You have recently been assigned the task of developing promotional techniques to introduce your company's new product, a Cajun chicken sandwich. Advertising spending is limited, so the introduction will include only some low-budget sales promotion techniques. Write a sales promotion plan that will increase awareness of your new sandwich and allow your customer base to try it risk-free.

LO 2

Discuss the most common forms of consumer sales promotion. Consumer forms of sales promotion include coupons and rebates, premiums, loyalty marketing programs, contests and sweepstakes, sampling, and point-of-purchase displays. Coupons are certificates entitling consumers to an immediate price reduction when they purchase a product or service. Coupons are a particularly good way to encourage product trial and brand switching. Similar to coupons, rebates provide purchasers with a price reduction, although it is not immediate. To receive a rebate, consumers generally must mail in a rebate form with a proof of purchase. Premiums offer an extra item or incentive to the consumer for buying a product or service. Premiums reinforce the consumer's purchase decision, increase consumption, and persuade nonusers to switch brands. Rewarding loyal customers is the basis of loyalty marketing programs. Loyalty programs are extremely effective at building long-term, mutually beneficial relationships between a company and its key customers. Contests and sweepstakes are generally designed to create interest, often to encourage brand switching. Because consumers perceive risk in trying new products, sampling is an effective method for gaining new customers. Finally, point-of-purchase displays set up at the retailer's location build traffic, advertise the product, and induce impulse buying.

2.1 Discuss how different forms of sales promotion can erode or build brand loyalty. If a company's objective is to enhance customer loyalty to its products, what sales promotion techniques will be most appropriate?

2.2 What forms of consumer sales promotion might induce impulse purchases? What forms of sales promotion are more effective at persuading consumers to switch brands?

2.3 Consider the different consumer sales promotion tools. Give an example of how each type of tool has influenced you to purchase—or purchase more of—a product or service.

ONLINE

2.4 Not everyone thinks supermarket shopper cards are a bargain. Go to **http:// www .nocards.org** and read several pages. Is the information on the site compelling? What do you think of shopper cards? You may want to use the Internet to research shopper cards in more detail before forming an opinion.

2.5 Contests and sweepstakes are very common in the entertainment industry. Radio stations have contests almost weekly (some daily); local television morning shows quiz viewers on trivia; even movies offer sweepstakes in conjunction with film previews and premiere nights. Think of a television or radio program unlikely to have contests or sweepstakes (things like *Cops, The View, Scooby Doo,* or your local classical music radio station, for example). Once you have chosen your program, design a contest or sweepstake to promote the show or the channel on which it airs. List the objectives and describe the rationale behind each part of your promotion.

2.6 How can uPromote.com (**http://www.upromote.com**) help you with your sales promotions efforts? What kind of marketing budget would you need to take advantage of its services? What kind of company would be best served by uPromote.com?

LO3 **List the most common forms of trade sales promotion.** Manufacturers use many of the same sales promotion tools used in consumer promotions, such as sales contests, premiums, and point-of-purchase displays. In addition, manufacturers and channel intermediaries use several unique promotional strategies: trade allowances, push money, training programs, free merchandise, store demonstrations, and meetings, conventions, and trade shows.

3.1 How does trade sales promotion differ from consumer sales promotion? How is it the same?

3.2 What are the main forms of trade sales promotion? Which type might be most enticing to a grocery store manager? To a buyer for a major electronics chain?

TEAM

3.3 Form a team of three to five students. As marketing managers, you are in charge of selling Dixie cups. Design a consumer sales promotion plan and trade sales promotion plan for your product. Incorporate at least three different promotion tools into each plan. Share your results with the other teams in the class.

LO4 **Describe personal selling.** Personal selling is direct communication between a sales representative and one or more prospective buyers in an attempt to influence each other in a purchase situation. Broadly speaking, all businesspeople use personal selling to promote themselves and their ideas. Personal selling offers several advantages over other forms of promotion. Personal selling allows salespeople to thoroughly explain and demonstrate a product. Salespeople have the flexibility to tailor a sales proposal to the needs and preferences of individual customers. Personal selling is more efficient than other forms of promotion because salespeople target qualified prospects and avoid wasting efforts on unlikely buyers. Personal selling affords greater managerial control over promotion costs. Finally, personal selling is the most effective method of closing a sale and producing satisfied customers.

4.1 Discuss the role of personal selling in promoting products. What advantages does personal selling offer over other forms of promotion?

4.2 What are the major advantages of personal selling to the company selling a product? What are the advantages to the person or company buying the product?

LO5 **Discuss the key differences between relationship selling and traditional selling.** Relationship selling is the practice of building, maintaining, and enhancing interactions with customers in order to develop long-term satisfaction through mutually beneficial partnerships. Traditional selling, on the other hand, is transaction focused. That is, the salesperson is most concerned with making onetime sales and moving on to the next prospect. Salespeople practicing relationship selling spend more time understanding a prospect's needs and developing solutions to meet those needs.

5.1 What are the key differences between relationship selling and traditional methods of selling? What types of products or services do you think would be conducive to relationship selling?

5.2 Based on the key differences between traditional and relationship selling, which type of sales approach would you use as a salesperson? Do the different approaches require different personal strengths or attributes?

LO6 **List the steps in the selling process.** The selling process is composed of seven basic steps: (1) generating leads, (2) qualifying leads, (3) approaching the customer and probing needs, (4) developing and proposing solutions, (5) handling objections, (6) closing the sale, and (7) following up.

WRITING

6.1 You are a new salesperson for a well-known medical software company, and one of your clients is a large group of physicians. You have just arranged an initial meeting with the office manager. Develop a list of questions you might ask at this meeting to uncover the group's specific needs.

6.2 What does sales follow-up entail? Why is it an essential step in the selling process, particularly from the perspective of relationship selling? How does it relate to cognitive dissonance?

ONLINE

6.3 How many ways can ZapData (**http://www.zapdata.com**) benefit salespeople? Which of its services would be most useful to marketing managers? Other businesspeople?

6.4 Consider each step in the selling process. Which steps could be conducted through technology (Internet, webinars, etc.)? Which are most important to handle "face-to-face"?

LO7

Describe the functions of sales management. Sales management is a critical area of marketing that performs several important functions. Sales managers set overall company sales goals and define the sales process most effective for achieving those goals. They determine sales force structure based on geographic, product, functional, or customer variables. Managers develop the sales force through recruiting and training. Sales management motivates the sales force through compensation planning, motivational tools, and effective sales leadership. Finally, sales managers evaluate the sales force through salesperson feedback and other methods of determining their performance.

7.1 What kinds of sales management opportunities are available at Amway and Quixtar? Use the companies' Web sites (**http://www.amway.com; http://www.quixtar.com**) to research one of these companies and determine its sales process, sales force structure, and how it recruits and trains its salespeople.

7.2 How does each of the sales management functions contribute to a successful, high-performing sales force?

Key Terms

consumer sales promotion	537
coupon	539
follow-up	554
frequent buyer program	540
lead generation (prospecting)	549
lead qualification	550
loyalty marketing program	540
needs assessment	551
negotiation	553
networking	550
personal selling	546
point-of-purchase display	543
preapproach	551
premium	540
push money	544
quota	555
rebate	540
referral	550
relationship selling (consultative selling)	547
sales presentation	552
sales process (sales cycle)	548
sales proposal	552
sampling	542
trade allowance	544
trade sales promotion	537

Exercises

APPLICATION EXERCISE

Have you ever waited forever to get a fast-food hamburger? Have you even been left to languish in a dressing room by a salesperson who left for a coffee break? If so, you already know that sales and customer service are integral parts of marketing. While you are working on this chapter, keep a journal of your personal sales and/or customer service experiences with local merchants. Don't ignore the details. Even such things as how crowded a store or restaurant is when you visit may affect your perceptions of the service you received.[50]

Activities

1. Keep your journal for a week, recording all sales and service transactions, if possible, on the day they occur.
2. At the end of the week, examine your journal, and pick the most noteworthy entry. Provide the basic information about the transaction: company where it occurred, type of transaction (purchase, return, complaint, etc.), type of good or service involved, and so forth.
3. Once you have the outlined the situation, evaluate the experience. Use the information about selling in this chapter as support for your evaluation. For example, did the salesperson seem to treat the situation as an individual, discrete transaction, or did he or she seem interested in building a relationship?
4. Finally, make recommendations as to how the company can improve its sales and/or service. Suggestions should be logical and achievable (meaning you have to consider the cost of implementing your suggestion).

ETHICS EXERCISE

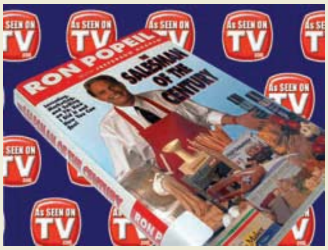
ETHICS

Sally Burke works for Hi-Tech Electronics. Her responsibilities include selecting items to advertise in her company's Sunday newspaper FSIs. One hot item is a 50-inch flat-panel

plasma TV. The list price is $4,999, but her manager tells her to advertise it at $3,999, since customers can apply for a $1,000 mail-in rebate. The advertised price has attracted many people to buy the TV; however, Sally has heard several complaints from customers who found the rebate process unusually complex and were denied a rebate because the manufacturer claimed they hadn't provided the required information. She would prefer to advertise the "real" list price, knowing that customers are not guaranteed to receive a rebate.

Questions

1. Is it unethical to advertise products at their post-rebate price in order to increase sales? Why or why not? What is another sales promotion method Hi-Tech Electronics could use to persuade customers to buy their plasma TV at the store?
2. Rebate programs are commonly used by electronics manufacturers because the rebates arouse consumers' interest in buying products; yet only half of purchasers ultimately claim their rebates. Is a rebate program itself unethical if the manufacturer knows consumers are unlikely to receive their money?
3. Visit a local electronics store—or Web site—and find a product being sold with a mail-in rebate offer. Are the rebate instructions clear? Would you take the time to complete the process?



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Case Study: Ron Popeil

RON POPEIL WHEELS, DEALS, HAS MASS APPEAL

At age 71, Ron Popeil is an avid inventor, tireless entrepreneur, clever marketer, and master salesman all in one. He just happens to be an American icon, too. The godfather of the infomercial, Popeil even has his famous Veg-O-Matic on display in the Smithsonian Institution as an American cultural artifact. His other famous products include the food dehydrator, the Ronco spray gun and the Popeil Pocket Fisherman.

As a teenager, Popeil helped his father sell his kitchen gadgets at local Woolworth's and later, in the 1950s, on the Chicago fair circuit. That is probably why his famous shtick, which included such memorable catch phrases as "But wait, there's more," "priced so low," and "Operators are standing by," always seemed like a blend between sincere eccentric inventor and excitable carnival barker. The combination suited him well and brought him enough financial success that he could afford to take his act to television. In the 1960s, he incorporated Ronco, and its name became synonymous with gadgets like the smokeless ashtray and Mr. Microphone.

Regardless of the product he is selling or the catchy pitch phrases he invents on the fly to sell them, Popeil is always sincere. "The easiest thing to do in the world is to sell a product I believe in," he has said. "If I spent two years creating a product, conceiving it, tinkering with it, I can get up and sell it. Who can sell it better than the guy who invented it?" Len Green, a professor in entrepreneurship at Babson University, says, "Ron is one of a kind. He is different from the rest because he not only invents, he sells. Most entrepreneurs come up with a concept and then give it to others to manufacture or sell. He's his own best salesman."

Though Popeil has suffered his fair share of flops, like spray-on hair and a brief bankruptcy in 1987, he has always managed to bounce back. Returning from bankruptcy, he relaunched the popular food dehydrator in 1990, and eight years later he designed and sold his most successful product ever, the Showtime rotisserie BBQ. Having sold over seven million units for four installments of $39.95 each, the rotisserie alone has grossed over $1 billion in sales. During the taping of the infomercial for that product, the live studio audience was treated to yet another of Popeil's catch phrases that has become part of the fabric of American speech. "Just set it and forget it!" is now used to sell all kinds of non-Popeil products from VCRs and digital video recorders to ovens and coffee makers.

Through the medium of television, Popeil was able to reach tens of millions of people. With an innate ability to invent or improve on everyday household products, his live product demonstrations captured the imaginations and dollars of generations of consumers. In 1976, he was even the subject of what was probably Dan Aykroyd's most famous bit on *Saturday Night Live.* Parodying Popeil, Aykroyd hawked "Rovco's Super Bass-O-Matic '76," which was capable of turning a bass or any other "small aquatic creature" into liquid without any "scaling, cutting or gutting."

Having recently sold Ronco to an investment group for over $55 million and accumulated a personal net worth of over $100 million, Popeil has had the last laugh. He will continue to serve as a product developer, pitchman, and consultant for the new company and already promises an even bigger hit than the Showtime rotisserie. Having identified a market of over 20 million Americans who fry turkeys every year, Popeil says he has a new fryer on the way that will make it possible to safely fry a 20-pound turkey in 70 minutes—indoors. Given that he has created over 150 products and invented personal selling via the mass marketing medium, there is little reason to doubt him.

As Barbara Gross, professor of marketing at California State University, Northridge, states, "His success speaks for itself; probably that has more to do with his personality. He's comfortable and sincere. He comes across like he really believes in it. When you hear him talk, you never feel like he's lying to you."[51]

Questions

1. What does Ron Popeil bring to personal selling that makes him so effective?
2. What trade sales promotion tools does he use? Why does he use sales promotion tools when he is selling direct to consumers?
3. Explain how Popeil's selling tactics allow him to achieve the desired objectives of sales promotions.
4. Do you think it is likely that America will ever see someone like Ron Popeil in the future? Why or why not?

Company Clips

VANS—OFF THE WALL PROMOTIONS

Steve VanDorn, son of the founder, is the self-proclaimed "ambassador of fun" at Vans. Because Vans doesn't want to discount its products or lower prices, it has to find other ways to create value for consumers. So, to keep the brand energized, the company is constantly developing promotions that can only be described as fun, an important element for attracting trendsetting customers. The core of Vans's strategy revolves around unique and authentic contests and giveaways. The company relies on word-of-mouth advertising and credible personal selling. In this video segment, Vans marketers explain how they use Web sites, contests, giveaways, and athletic events to attract and keep customers.

Questions

1. How does Vans use giveaways and contests to market its products? Why do these strategies work so well for Vans?
2. How does Vans approach recruiting and training its sales force?
3. How have trade shows changed in recent years? What is Vans's main goal at trade shows today?

Marketing & You Results

High scores on this poll indicate a preference for using coupons, which may indicate that you are a comparison shopper. If your score was low, you probably don't see any economic benefits to using coupons, and you're likely not a comparison shopper. Instead, you probably prefer to buy what you want regardless of any coupon promotion.

END OF PART 5

Marketing Miscue

Dolce & Gabbana Pulls Ads

Dolce & Gabbana is a world-renowned luxury goods retailer. Founded in 1985 by Domenico Dolce and Stefano Gabbana, the Italian fashion house has operations in Luxembourg, New York, Tokyo, Hong Kong, Rome, London, Paris, Barcelona, Düsseldorf, and Shanghai. With over 3,000 employees and a retail network of 87 stores and 11 factory outlets, the company reported 2006 year-ending sales of 1,151.3 million euros for its two brands, Dolce & Gabbana and D&G Dolce & Gabbana.

By early 2007, the company had begun receiving harsh criticism for some of its print ads. British ads appearing in *The Times* and *Daily Telegraph* newspapers in October of 2006 were condemned publicly due to complaints that the ads glorified knife and gun crime. One of the advertisements showed two men threatening a man in a chair while another man lay on the floor with a head wound. The other ad focused upon two men supporting a wounded woman who was holding a knife. The Advertising Standards Authority, an independent regulatory agency in the United Kingdom, reported that 166 people had complained about the ads.

Dolce & Gabbana responded to the complaints by saying that the pictures were designed to evoke the Napoleonic period of art, emphasizing the theatrical effects of the genre, and that the ads had appeared in newspapers and magazines around the world. The company claimed that the ads had only drawn complaints within the United Kingdom. Interestingly, the ad had been positioned opposite a story about knife violence. The Advertising Standards Authority agreed with the public outcry and said that the company had acted irresponsibly and that it had breached standards of good taste. However, the agency did not go so far as to ban the ads from publication.

A little more than a month after the exchange with the British advertising authority, a Dolce & Gabbana ad appeared in various magazines and newspapers that sparked worldwide controversy. The ad showed a woman clothed in a tight black dress and spiked heels lying on her back as a bare-chested man held her down by the wrists. Four other men were pictured observing the scene. According to a Dolce & Gabbana spokesperson, the ad was meant to portray an erotic dream or sexual game. The ad was promoting the company's spring/summer 2007 ready-to-wear collection.

Critics claimed that the ad provoked images of gang rape and violence against women, particularly since the woman was portrayed with an unsmiling, blank look on her face, and the four male observers appeared to be sneering. After receiving complaints from the Women's Institute of Spain and consumer advocates, Spain's Labour and Social Affairs Ministry said that the ad should be illegal since it was humiliating to women. In supporting this claim, a spokesperson for the Spanish Labor Ministry's Women's Institute said that the ad trivialized violence against women and that the ad might convince a violent person that he or she was justified in using force against women. In response to the Spanish concerns, Dolce & Gabbana said that Spain was "behind the times" and that it would pull all of its advertising from Spain.

Authorities in other countries were not far behind that of Spain, however, in condemning what many saw as Dolce & Gabbana's gang-rape ad. Thirteen Italian senators and the Italian minister for Equal Opportunity appealed to Italy's Advertising Self-Discipline Institute to ban the ad. Additionally, the textile workers' division of Italy's largest trade union, CGIL, was set to boycott Dolce & Gabbana products on International Women's Day on March 8, 2008. The boycott was in conjunction with concerns raised by Amnesty International in Italy that the company was condoning violence against women. In the United States, the president of the National Organization for Women said that the ad provoked things that should not be provoked. Following the protests, Dolce & Gabbana pulled the ad from further publication.

Questions

1. While controversial, the ads created considerable buzz for Dolce & Gabbana. Given this, was the controversy a mistake?
2. Ad opponents suggested that Dolce & Gabbana was provoking/justifying violence in both of these ads. What is Dolce & Gabbana's role in this social issue?

Critical Thinking Case

Vector Marketing Corporation—Recruitment and Technology

Vector Marketing Corporation is a direct sales firm that markets Cutco Cutlery, a line of high quality kitchen cutlery, kitchen accessories, and sporting knives. Since its inception, Vector Marketing has offered college students and graduates career opportunities in direct selling and sales management. Historically, the company recruited sales representatives via direct mail campaigns and personal recommendations. However, the technological savviness of today's young requires the company to adapt its methods so that it can attract sales representatives in the age of technology.

Vector Marketing Corporation

Vector Marketing is the sole distributor of Cutco Cutlery. Made in Olean, New York, since 1949, Cutco is proud to be an American-made product with more than 15 million Cutco owners in the United States. Both Vector Marketing and Cutco Cutlery Corporation are wholly owned subsidiaries of Alcas Corporation.

With annual sales over $197 million, Vector Marketing has over 300 offices across the United States and Canada. In the United States, the company is divided into six regions (Northeast, Midwest, Eastern, Central, Southwest, and Western). The company's corporate vision is "to become the largest, most respected and widely recognized cutlery company in the world."

Career Progression

The company has a "promote from within" policy, which means that all office managers started as sales representatives and have developed the field experience and professional insight needed to develop talents in others. Although the majority of Vector's sales representatives are college students, the company does accept applications from anyone over the age of 17. A representative's primary activities include:

- Setting appointments with potential customers through personal contacts and referrals.
- Presenting Cutco products to prospective customers and taking orders.
- Reviewing personal performance with the local office manager through meetings and over the phone.
- Attending advanced training sessions and conferences that are regularly offered to increase knowledge and productivity.

There is no previous experience required for the entry level sales position. New representatives participate in training, normally over three consecutive days, at a local Vector Marketing office. The initial training seminar is designed to instill confidence in the trainee who may have limited work experience.

Qualified sales representatives have the opportunity to advance into management roles while still pursuing their education. Vector Marketing has a clear career path that provides advancement into positions with increasing responsibility.

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Attracting Sales Representatives in the Age of Technology

Sales force training programs highlight the role technology can play when it comes to improving individual sales productivity. With Vector Marketing's unique college student sales force, however, the company faces a different technology issue. That is, what is the best way to attract and recruit an age demographic that is essentially wedded to technology via their cell phones, PDAs, and computers? Is direct mail a thing of the past with this demographic?

Questions

1. Relate the steps in the selling process to the recruiting effort utilized by Vector Marketing.
2. Brainstorm some ways in which Vector Marketing could use technology to reach out to college students to interest them in its sales program.

P A R T 6

Pricing Decisions

WHAT'S INSIDE

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CHAPTER 19

Pricing Concepts

Learning Outcomes

- LO 1 Discuss the importance of pricing decisions to the economy and to the individual firm
- LO 2 List and explain a variety of pricing objectives
- LO 3 Explain the role of demand in price determination
- LO 4 Understand the concept of yield management systems
- LO 5 Describe cost-oriented pricing strategies
- LO 6 Demonstrate how the product life cycle, competition, distribution and promotion strategies, guaranteed price matching, customer demands, the Internet, and perceptions of quality can affect price

LO 1

The Importance of Price

Price means one thing to the consumer and something else to the seller. To the consumer, it is the cost of something. To the seller, price is revenue, the primary source of profits. In the broadest sense, price allocates resources in a free-market economy. With so many ways of looking at price, it's no wonder that marketing managers find the task of setting prices a challenge.

WHAT IS PRICE?

price
That which is given up in an exchange to acquire a good or service.

revenue
The price charged to customers multiplied by the number of units sold.

profit
Revenue minus expenses.

Price is that which is given up in an exchange to acquire a good or service. Price is typically the money exchanged for the good or service. It may also be time lost while waiting to acquire the good or service. Standing in long lines at the airport first to check in and then to get through the security checkpoint procedures is a cost. In fact, these delays are one reason more people are selecting alternative modes of transportation for relatively short trips. Price might also include "lost dignity" for individuals who lose their jobs and must rely on charity to obtain food and clothing.

Consumers are interested in obtaining a "reasonable price." "Reasonable price" really means "perceived reasonable value" at the time of the transaction. One of the authors of this textbook bought a fancy European-designed toaster for about $45. The toaster's wide mouth made it possible to toast a bagel, warm a muffin, and, with a special $15 attachment, make a grilled sandwich. The author felt that a toaster with all these features surely must be worth the total price of $60. But after three months of using the device, toast that burned around the edges and remained raw in the middle lost its appeal. The disappointed buyer put the toaster in the attic. Why didn't he return it to the retailer? Because the boutique had gone out of business, and no other local retailer carried the brand. Also, there was no U.S. service center. Remember, the price paid is based on the satisfaction consumers expect to receive from a product and not necessarily the satisfaction they actually receive.

Price can relate to anything with perceived value, not just money. When goods and services are exchanged, the trade is called barter. For example, if you exchange this book for a chemistry book at the end of the term, you have engaged in barter. The price you paid for the chemistry book was this textbook.

Marketing & You

Using the following scale, enter your opinion of the following items on the lines provided.

1	2	3	4	5	6	7
Strongly disagree						Strongly agree

— People notice when you buy the most expensive brand of a product.

— Buying the most expensive brand of a product makes me feel classy.

— I enjoy the prestige of buying a high-priced brand.

— It says something to people when you buy the high-priced version of a product.

— I have purchased the most expensive brand of a product just because I knew other people would notice.

— Even for a relatively inexpensive product, I think that buying a costly brand is impressive.

Total your score, and find out what it means after you read the chapter.

THE IMPORTANCE OF PRICE TO MARKETING MANAGERS

Prices are the key to revenues, which in turn are the key to profits for an organization. **Revenue** is the price charged to customers multiplied by the number of units sold. Revenue is what pays for every activity of the company: production, finance, sales, distribution, and so on. What's left over (if anything) is **profit**. Managers usually strive to charge a price that will earn a fair profit.

To earn a profit, managers must choose a price that is not too high or too low, a price that equals the perceived value to target consumers. If, in consumers' minds, a price is set too high, the perceived value will be less than the cost, and sales opportunities will be lost. Many mainstream purchasers of cars, sporting goods, CDs, tools, wedding gowns, and computers are buying "used or preowned" items to get a better deal. Pricing a new product too high may give some shoppers an incentive to go to a "preowned" or consignment retailer. Lost sales mean lost revenue. Conversely, if a price is too low, the consumer may perceive it as a great value, but the firm loses revenue it could have earned.

Trying to set the right price is one of the most stressful and pressure-filled tasks of the marketing manager, as trends in the consumer market attest:

- Confronting a flood of new products, potential buyers carefully evaluate the price of each one against the value of existing products.
- The increased availability of bargain-priced private and generic brands has put downward pressure on overall prices.
- Many firms are trying to maintain or regain their market share by cutting prices. For example, Ikea has gained market share in the furniture industry by aggressively cutting prices.
- The Internet has made comparison shopping easier.

In the organizational market, where customers include both governments and businesses, buyers are also becoming more price sensitive and better informed. Computerized information systems enable the organizational buyer to compare price and performance with great ease and accuracy. Improved communication and the increased use of direct marketing and computer-aided selling have also opened up many markets to new competitors. Finally, competition in general is increasing, so some installations, accessories, and component parts are being marketed like indistinguishable commodities.

REVIEW LEARNING OUTCOME

LO 1 Discuss the importance of pricing decisions to the economy and to the individual firm

Price × Sales Unit = Revenue

Revenue – Costs = Profit

Profit drives growth, salary increases, and corporate investment.

LO 2 Pricing Objectives

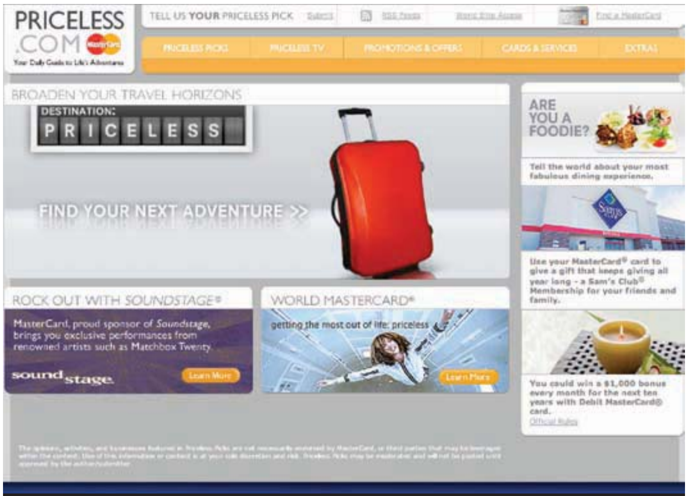
To survive in today's highly competitive marketplace, companies need pricing objectives that are specific, attainable, and measurable. Realistic pricing goals then require periodic monitoring to determine the effectiveness of the company's strategy. For convenience, pricing objectives can be divided into three categories: profit oriented, sales oriented, and status quo.

PROFIT-ORIENTED PRICING OBJECTIVES

Profit-oriented objectives include profit maximization, satisfactory profits, and target return on investment. A brief discussion of each of these objectives follows.

Profit Maximization

Profit maximization means setting prices so that total revenue is as large as possible relative to total costs. (A more theoretically precise definition and explanation of profit maximization appear later in the chapter.) Profit maximization does not always signify unreasonably high prices, however. Both price and profits depend on the type of competitive environment a firm faces, such as whether it is in a monopoly position (being the only seller) or in a much more competitive situation. Also, remember



COURTESY, MASTERCARD

Facing heavy competition from Visa and American Express, Mastercard's "priceless" campaign was meant to position it as the credit card company that was in a relationship with its customer. The ads suggested that Mastercard understood what its customers wanted—the intangibles and experiences that make life "priceless" AND the tangible things that they could purchase.

that a firm cannot charge a price higher than the product's perceived value. Many firms do not have the accounting data they need for maximizing profits. It is easy to say that a company should keep producing and selling goods or services as long as revenues exceed costs. Yet it is often hard to set up an accounting system that can accurately determine the point of profit maximization.

Sometimes managers say that their company is trying to maximize profits—in other words, trying to make as much money as possible. Although this goal may sound impressive to stockholders, it is not good enough for planning. The statement "We want to make all the money we can" is vague and lacks focus. It gives management license to do just about anything it wants to do.

In attempting to maximize profits, managers can try to expand revenue by increasing customer satisfaction, or they can attempt to reduce costs by operating more efficiently. A third possibility is to attempt to do both. Recent research has shown that striving to enhance customer satisfaction leads to greater profitability (and customer satisfaction) than following a cost reduction strategy or attempting to do both.[1] This means that companies should consider allocating more resources to customer service initiatives, loyalty programs, and customer relationship management programs and allocating fewer resources to programs that are designed to improve efficiency and reduce costs. Both types of programs, of course, are critical to the success of the firm.

Satisfactory Profits

Satisfactory profits are a reasonable level of profits. Rather than maximizing profits, many organizations strive for profits that are satisfactory to the stockholders and management—in other words, a level of profits consistent with the level of risk an organization faces. In a risky industry, a satisfactory profit may be 35 percent. In a low-risk industry, it might be 7 percent. To maximize profits, a small-business owner might have to keep his or her store open seven days a week. However, the owner might not want to work that hard and might be satisfied with less profit.

Target Return on Investment

return on investment (ROI) Net profit after taxes divided by total assets.

The most common profit objective is a target **return on investment (ROI),** sometimes called the firm's return on total assets. ROI measures management's overall effectiveness in generating profits with the available assets. The higher the firm's ROI, the better off the firm is. Many companies—including DuPont, General Electric, Navistar, ExxonMobil, and Union Carbide—use a target ROI as their main pricing goal. In summary, ROI is a percentage that puts a firm's profits into perspective by showing profits relative to investment.

Return on investment is calculated as follows:

$$\text{Return on investment} = \frac{\text{Net profits after taxes}}{\text{Total assets}}$$

Assume that in 2009 Johnson Controls had assets of \$4.5 million, net profits of \$550,000, and a target ROI of 10 percent. This was the actual ROI:

$$\text{ROI} = \frac{\$550{,}000}{\$4{,}500{,}000}$$
$$= 12.2 \text{ percent}$$

As you can see, the ROI for Johnson Controls exceeded its target, which indicates that the company prospered in 2009.

Comparing the 12.2 percent ROI with the industry average provides a more meaningful picture, however. Any ROI needs to be evaluated in terms of the competitive environment, risks in the industry, and economic conditions. Generally speaking, firms seek ROIs in the 10 to 30 percent range. For example, General Electric seeks a 25 percent ROI, whereas Alcoa, Rubbermaid, and most major pharmaceutical companies strive for a 20 percent ROI. In some industries such as the grocery industry, however, a return of under 5 percent is common and acceptable.

A company with a target ROI can predetermine its desired level of profitability. The marketing manager can use the standard, such as 10 percent ROI, to determine whether a particular price and marketing mix are feasible. In addition, however, the manager must weigh the risk of a given strategy even if the return is in the acceptable range.

SALES-ORIENTED PRICING OBJECTIVES

Sales-oriented pricing objectives are based either on market share or on dollar or unit sales. The effective marketing manager should be familiar with these pricing objectives.

Market Share

market share
A company's product sales as a percentage of total sales for that industry.

Market share is a company's product sales as a percentage of total sales for that industry. Sales can be reported in dollars or in units of product. It is very important to know whether market share is expressed in revenue or units because the results may be different. Consider four companies competing in an industry with 2,000 total unit sales and total industry revenue of $4 million (see Exhibit 19.1). Company A has the largest unit market share at 50 percent, but it has only 25 percent of the revenue market share. In contrast, company D has only a 15 percent unit share but the largest revenue share: 30 percent. Usually, market share is expressed in terms of revenue and not units.

Many companies believe that maintaining or increasing market share is an indicator of the effectiveness of their marketing mix. Larger market shares have indeed often meant higher profits, thanks to greater economies of scale, market power, and ability to compensate top-quality management. Conventional wisdom also says that market share and return on investment are strongly related. For the most part they are; however, many companies with low market share survive and even prosper. To succeed with a low market share, companies need to compete in industries with slow growth and few product changes—for instance, industrial component parts and supplies. Otherwise, they must vie in an industry that makes frequently bought items, such as consumer convenience goods.

The conventional wisdom about market share and profitability isn't always reliable, however. Because of extreme competition in some industries, many market share leaders either do not reach their target ROI or actually lose money. Freightliner, a manufacturer of heavy trucks, aggressively fought for market share

Exhibit 19.1

Two Ways to Measure Market Share (Units and Revenue)

Company	Units Sold	Unit Price	Total Revenue	Unit Market Share	Revenue Market Share
A	1,000	$1.00	$1,000,000	50%	25%
B	200	4.00	800,000	10	20
C	500	2.00	1,000,000	25	25
D	300	4.00	1,200,000	15	30
Total	2,000		$4,000,000		

gains during the past decade. Though Freightliner grew to become the market leader with a 36 percent market share, its profits suffered. It lost hundreds of millions of dollars and slashed 8,000 jobs in an effort to cut costs.[2] The personal computer and food industries have also had this problem. Procter & Gamble switched from market share to ROI objectives after realizing that profits don't automatically follow from a large market share. PepsiCo says its new Pepsi challenge is to be number one in share of industry profit, not in share of sales volume.

Still, the struggle for market share can be all-consuming for some companies. For years, Intel Corporation has had a "monopoly grip" on the chip market. Advanced Micro Devices (AMD) has had a singular focus of breaking that grip. Through acquisitions, advanced technology, and aggressive pricing, AMD attained 19 percent market share in 2007. Together, the two companies account for 99 percent of the chip market for the X86 processor. AMD's objective is to grow its total chip market share to 30 percent over the next several years.[3]

Research organizations like A. C. Nielsen and Information Resources, Inc., provide excellent market share reports for many different industries. These reports enable companies to track their performance in various product categories over time.

Sales Maximization

Rather than strive for market share, sometimes companies try to maximize sales. A firm with the objective of maximizing sales ignores profits, competition, and the marketing environment as long as sales are rising.

If a company is strapped for funds or faces an uncertain future, it may try to generate a maximum amount of cash in the short run. Management's task when using this objective is to calculate which price-quantity relationship generates the greatest cash revenue. Sales maximization can also be effectively used on a temporary basis to sell off excess inventory. It is not uncommon to find Christmas cards, ornaments, and other seasonal items discounted at 50 to 70 percent off retail prices after the holiday season. In addition, management can use sales maximization for year-end sales to clear out old models before introducing the new ones.

Maximization of cash should never be a long-run objective because cash maximization may mean little or no profitability. Without profits, a company cannot survive.

STATUS QUO PRICING OBJECTIVES

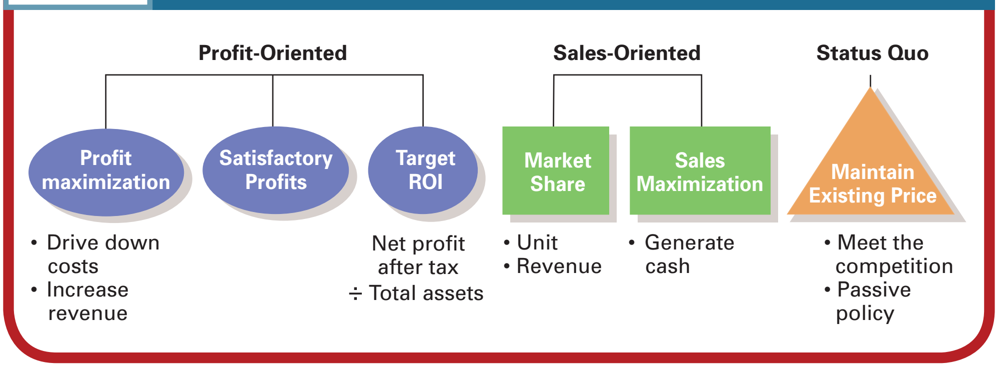
status quo pricing
A pricing objective that maintains existing prices or meets the competition's prices.

Status quo pricing seeks to maintain existing prices or to meet the competition's prices. This third category of pricing objectives has the major advantage of requiring little planning. It is essentially a passive policy.

Often firms competing in an industry with an established price leader simply meet the competition's prices. These industries typically have fewer price wars than those with direct price competition. In other cases, managers regularly shop competitors' stores to ensure that their prices are comparable. Target's middle managers may visit competing Wal-Mart stores to compare prices and then make adjustments.

REVIEW LEARNING OUTCOME

LO 2 List and explain a variety of pricing objectives



LO3 The Demand Determinant of Price

demand The quantity of a product that will be sold in the market at various prices for a specified period.

supply The quantity of a product that will be offered to the market by suppliers at various prices for a specified period.

After marketing managers establish pricing goals, they must set specific prices to reach those goals. The price they set for each product depends mostly on two factors: the demand for the good or service and the cost to the seller for that good or service. When pricing goals are mainly sales oriented, demand considerations usually dominate. Other factors, such as distribution and promotion strategies, perceived quality, demands of large customers, the Internet, and stage of the product life cycle, can also influence price.

THE NATURE OF DEMAND

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Demand is the quantity of a product that will be sold in the market at various prices for a specified period. The quantity of a product that people will buy depends on its price. The higher the price, the fewer goods or services consumers will demand. Conversely, the lower the price, the more goods or services they will demand.

This trend is illustrated in Exhibit 19.2(a), which graphs the demand per week for fruit smoothies at a local retailer at various prices. This graph is called a demand curve. The vertical axis of the graph shows different prices of fruit smoothies, measured in dollars per package. The horizontal axis measures the quantity of fruit smoothies that will be demanded per week at each price. For example, at a price of $2.50, 50 smoothies will be sold per week; at $1.00, consumers will demand 120 smoothies—as the demand schedule in Exhibit 19.2(b) shows.

The demand curve in Exhibit 19.2 slopes downward and to the right, which indicates that more fruit smoothies are demanded as the price is lowered. In other words, if smoothie makers put a greater quantity on the market, then their hope of selling all of it will be realized only by selling it at a lower price.

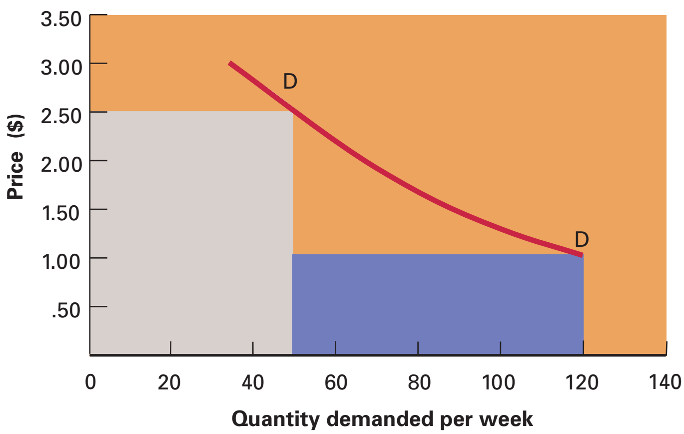
One reason more is sold at lower prices than at higher prices is that lower prices bring in new buyers. This fact might not be so obvious with fruit smoothies, but consider the example of steak. As the price of steak drops lower and lower, some people who have not been eating steak will probably start buying it rather than hamburger. With each reduction in price, existing customers may also buy extra amounts. Similarly, if the price of smoothies falls low enough, some people will buy more than they have bought in the past.

Supply is the quantity of a product that will be offered to the market by a supplier or suppliers at various prices for a specified period. Exhibit 19.3(a) illustrates the resulting supply curve for fruit smoothies. Unlike the falling demand curve, the supply curve for smoothies slopes upward and to the right. At higher prices, smoothie makers will obtain more resources (apples, peaches, strawberries) and make more smoothies. If the price consumers are willing to pay for smoothies increases, producers can afford to buy more ingredients.

Exhibit 19.2

Demand Curve and Demand Schedule for Fruit Smoothies

(a) Demand curve



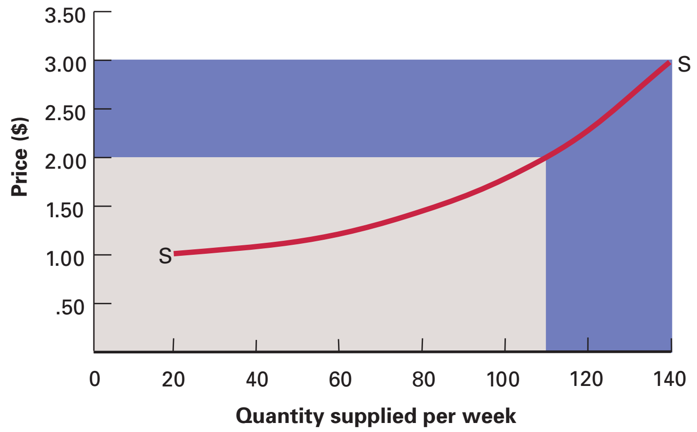
(b) Demand schedule

Price per package of fruit smoothies ($)	Packages of fruit smoothies demanded per week
3.00	35
2.50	50
2.00	65
1.50	85
1.00	120

Exhibit 19.3

Supply Curve and Supply Schedule for Fruit Smoothies

(a) Supply curve



(b) Supply schedule

Price per package of fruit smoothies ($)	Packages of fruit smoothies supplied per week
3.00	140
2.50	130
2.00	110
1.50	85
1.00	25

Output tends to increase at higher prices because a smoothie shop can sell more smoothies and earn greater profits. The supply schedule in Exhibit 19.3(b) shows that at $2 suppliers are willing to place 110 smoothies on the market, but that they will offer 140 drinks at a price of $3.

HOW DEMAND AND SUPPLY ESTABLISH PRICES

At this point, let's combine the concepts of demand and supply to see how competitive market prices are determined. So far, the premise is that if the price is X, then consumers will purchase Y amount of smoothie. How high or low will prices actually go? How many drinks will be produced? How many will be consumed? The demand curve cannot predict consumption, nor can the supply curve alone forecast production. Instead, we need to look at what happens when supply and demand interact—as shown in Exhibit 19.4.

At a price of $3, the public would demand only 35 smoothies. However, suppliers stand ready to place 140 smoothies on the market at this price (data from the demand and supply schedules). If they do, they would create a surplus of 105 smoothies. How does a merchant eliminate a surplus? It lowers the price.

price equilibrium
The price at which demand and supply are equal.

elasticity of demand
Consumers' responsiveness or sensitivity to changes in price.

elastic demand
A situation in which consumers buy significantly more or less of a product when its price changes.

inelastic demand
A situation in which an increase or a decrease in price will not significantly affect demand for the product.

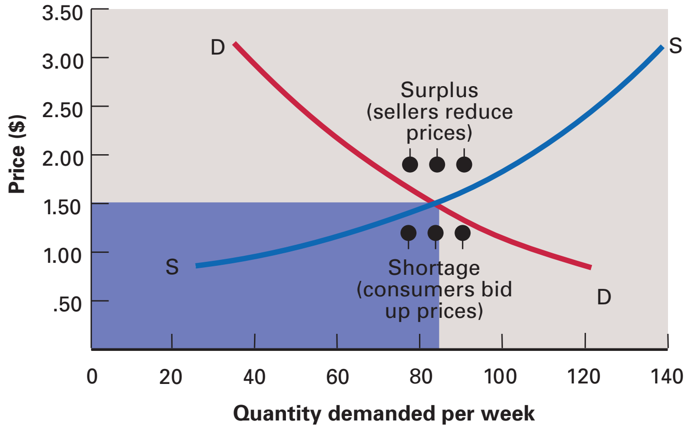
At a price of $1, 120 smoothies would be demanded, but only 25 would be placed on the market. A shortage of 95 units would be created. If a product is in short supply and consumers want it, how do they entice the seller to part with one unit? They offer more money—that is, pay a higher price.

Now let's examine a price of $1.50. At this price, 85 smoothies are demanded and 85 are supplied. When demand and supply are equal, a state called price equilibrium is achieved. A temporary price below equilibrium—say, $1.00—results in a shortage because at that price the demand for fruit smoothies is greater than the available supply. Shortages put upward pressure on price. As long as demand and supply remain the same, however, temporary price increases or decreases tend to return to equilibrium. At equilibrium, there is no inclination for prices to rise or fall.

An equilibrium price may not be reached all at once. Prices may fluctuate during a trial-and-error period as the market for a good or service moves toward equilibrium. Sooner or later, however, demand and supply will settle into proper balance.

Exhibit 19.4

Equilibrium Price for Fruit Smoothies



ELASTICITY OF DEMAND

To appreciate demand analysis, you should understand the concept of elasticity. Elasticity of demand refers to consumers' responsiveness or sensitivity to changes in price. Elastic demand occurs when consumers buy significantly more or less of a product when the price changes. Conversely, inelastic demand means that an increase or a decrease in price will not significantly affect demand for the product.

Elasticity over the range of a demand curve can be measured by using this formula:

$$\text{Elasticity (E)} = \frac{\text{Percentage change in quantity demanded of good A}}{\text{Percentage change in price of good A}}$$

If E is greater than 1, demand is elastic.
If E is less than 1, demand is inelastic.
If E is equal to 1, demand is unitary.

unitary elasticity
A situation in which total revenue remains the same when prices change.

Unitary elasticity means that an increase in sales exactly offsets a decrease in prices, so total revenue remains the same.

Elasticity can be measured by observing these changes in total revenue:

If price goes down and revenue goes up, demand is elastic.
If price goes down and revenue goes down, demand is inelastic.
If price goes up and revenue goes up, demand is inelastic.
If price goes up and revenue goes down, demand is elastic.
If price goes up or down and revenue stays the same, elasticity is unitary.

Exhibit 19.5(a) shows a very elastic demand curve. Decreasing the price of Apple iPhones from $300 to $200 increases sales from 18,000 units to 59,000 units. Revenue increases from $5.4 million ($300 × 18,000) to $11.8 million ($200 × 59,000). The price decrease results in a large increase in sales and revenue.

Exhibit 19.5(b) shows a completely inelastic demand curve. The state of Nevada dropped its used-car vehicle inspection fee from $20 to $10. The state continued to inspect about 400,000 used cars annually. Decreasing the price (inspection fee) 50 percent did not cause people to buy more used cars. Demand is completely inelastic for inspection fees, which are required by law. Thus, it also follows that Nevada could double the original fee to $40 and double the state's inspection revenues. People won't stop buying used cars if the inspection fee increases—within a reasonable range.

Exhibit 19.6 presents the demand curve and demand schedule for three-ounce bottles of Spring Break suntan lotion. Let's follow the demand curve from the highest price to the lowest and examine what happens to elasticity as the price decreases.

Inelastic Demand

The initial decrease in the price of Spring Break suntan lotion, from $5.00 to $2.25, results in a decrease in total revenue of $969 ($5,075 − $4,106). When price and total revenue fall, demand is inelastic. The decrease in price is much greater than the increase in suntan lotion sales (810 bottles). Demand is therefore not very flexible in the price range $5.00 to $2.25.

When demand is inelastic, sellers can raise prices and increase total revenue. Often items that are relatively inexpensive but convenient tend to have inelastic demand.

Elastic Demand

In the example of Spring Break suntan lotion, shown in Exhibit 19.6, when the price is dropped from $2.25

Exhibit 19.5

Elasticity of Demand for Apple iPhones and Auto Inspection Stickers

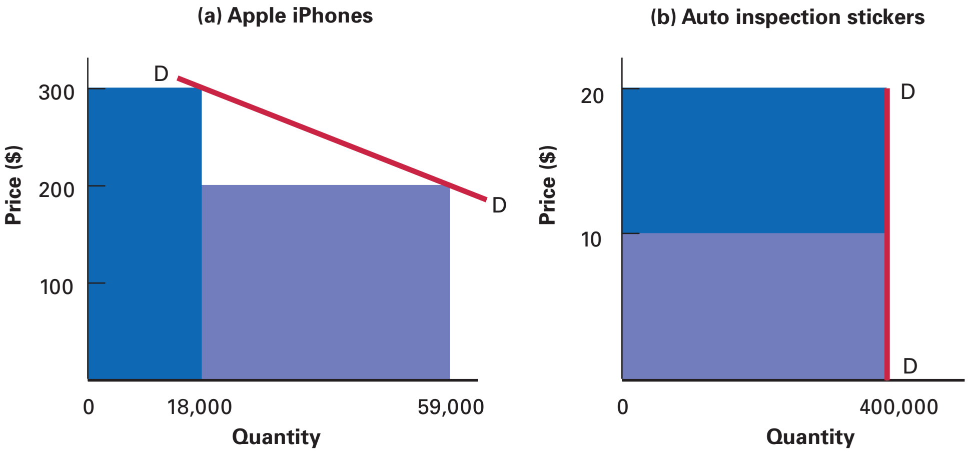
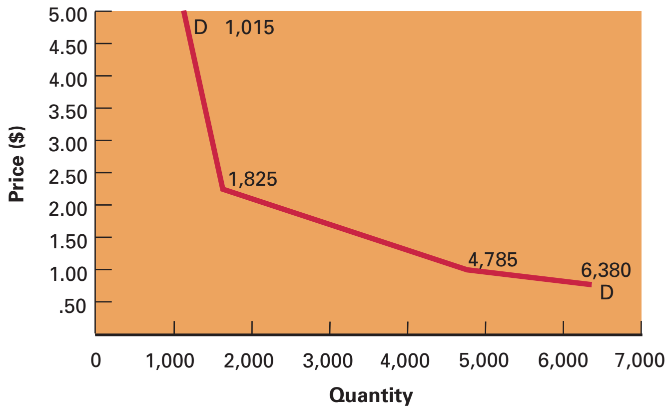


Exhibit 19.6

Demand for Three-Ounce Bottles of Spring Break Suntan Lotion

(a) Demand curve



(b) Demand schedule

Price ($)	Quantity demanded	Total revenue (price × quantity)	Elasticity
5.00	1,015	$5,075	Inelastic
2.25	1,825	4,106	
1.00	4,785	4,785	Elastic
0.75	6,380	4,785	Unitary

to $1.00, total revenue increases by $679 ($4,785 − $4,106). An increase in total revenue when price falls indicates that demand is elastic. Let's measure Spring Break's elasticity of demand when the price drops from $2.25 to $1.00 by applying the formula presented earlier:

$$E = \frac{\text{Change in quantity/(Sum of quantities/2)}}{\text{Change in price/(sum of prices/2)}}$$

$$= \frac{(4{,}785 - 1{,}825)/[(1{,}825 + 4{,}785)/2]}{(2.25 - 1.00)/[(2.25 + 1.00)/2]}$$

$$= \frac{2{,}960/3{,}305}{1.25/1.63}$$

$$= \frac{.896}{.767}$$

$$= 5\ 1.17$$

Because E is greater than 1, demand is elastic.

Factors That Affect Elasticity

Several factors affect elasticity of demand, including the following:

- *Availability of substitutes:* When many substitute products are available, the consumer can easily switch from one product to another, making demand elastic. The same is true in reverse: a person with complete renal failure will pay whatever is charged for a kidney transplant because there is no substitute. Interestingly, Bose stereo equipment is priced 300 to 500 percent higher than other stereo brands. Yet consumers are willing to pay the price because they perceive the equipment as being so superior to other brands that there is no acceptable substitute.
- *Price relative to purchasing power:* If a price is so low that it is an inconsequential part of an individual's budget, demand will be inelastic. For example, if the price of salt doubles, consumers will not stop putting salt and pepper on their eggs because salt is cheap anyway.
- *Product durability:* Consumers often have the option of repairing durable products rather than replacing them, thus prolonging their useful life. If a person plans to buy a new car and prices suddenly begin to rise, he or she may elect to fix the old car and drive it for another year. In other words, people are sensitive to the price increase, and demand is elastic.
- *A product's other uses:* The greater the number of different uses for a product, the more elastic demand tends to be. If a product has only one use, as may be true of a new medicine, the quantity purchased probably will not vary as price varies. A person will consume only the prescribed quantity, regardless of price. On the other hand, a product like steel has many possible applications. As its price falls, steel becomes more economically feasible in a wider variety of applications, thereby making demand relatively elastic.

COURTESY OF CHAPEL HOUSE PHOTOGRAPHY

One factor affecting price elasticity is the availability of substitutes. For example, many consumers do not think there is any substitute for Bose radio and stereo products. As a result, the price on Bose products is inelastic, even though they are priced at 300 to 500 percent above other stereo manufacturers' brands.

- *Rate of inflation:* Recent research has found that when a country's inflation rate (the rate at which the price level is rising) is high, demand becomes more elastic. In other words, rising price levels make consumers more price sensitive. The research also found that during inflationary periods consumers base their timing (when to buy) and quantity decisions on price promotions. This suggests that a brand gains additional sales or market share if the product is effectively promoted or if the marketing manager keeps the brand's price increases low relative to the inflation rate.[4]

Examples of both elastic and inelastic demand abound in everyday life. Recently, fans balked at high prices for concerts. Promoters lost money, and some shows including some by artists Christina Aguilera and Marc Anthony were canceled. This is price elasticity in action. On the other hand, demand for some tickets was highly inelastic. The Rolling Stones are still selling out concerts with tickets priced at up to $400.[5]

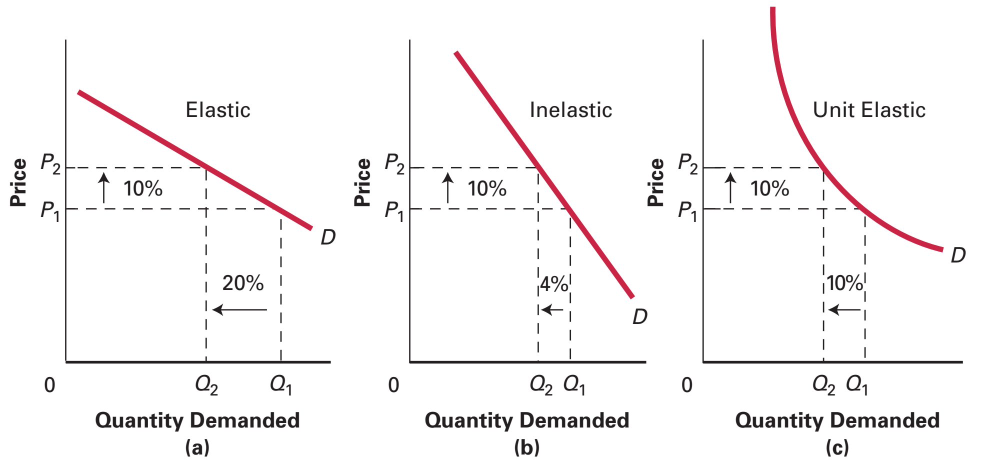
Pricing Power

For many companies most pricing power vanished long ago. A lack of pricing power means that when a company tries to raise its prices, it loses sales volume as customers shift to low cost competitors or find a substitute product. Ultimately, many of these companies have had to lower prices again—sometimes dropping them even further than they were before the attempted price increase—in an effort to recapture lost share.

In contrast, pricing power means making a price increase stick. It means that demand is relatively inelastic for the product. How does a firm gain pricing power? One strategy is to produce something radically new, and most importantly, better than the competition. Eric Soule had been waiting 15 months for this moment. The semiconductor engineer was about to launch a new chip, and he needed his pricing approved. In a conference room at Linear Technology Corp., Mr. Soule anxiously

REVIEW LEARNING OUTCOME

LO3 Explain the role of demand in price determination



What affects elasticity?
- Availability of subtitutes
- Price relative to purchasing power
- Product durability
- Product's other uses
- Inflation rate

Exhibit 19.7

Parker Hannifin's Strategy to Create Pricing Power

PRNEWSFOTO/PARKER HANNIFIN CORPORATION

Product Categories	Pricing Strategy Rationale	Price Increase (%)
Core products	Basic commodity in high volume with market competition	-3–5
Partially differentiated products (A)	Some differentiation to core product that meets wider market's needs in competitive market	0–5
Partially differentiated product (B)	Some differentiation to product or niche product with little or no market competition	0–9
System or differentiated products	Custom engineering to customer specifications that improves customer's productivity and profitability; some market competition	0–25
Classic or Special products	Custom-designed or unique product with no market competition	>25

Adapted from Timothy Aeppel's *Wall Street Journal* article, "Seeking Perfect Prices, CEO Tears Up the Rules," March 27, 2007, James Sagar's article "Pricing Strategy: Capture More Revenue," Marketing M.O. Consulting, online at **http://www.marketingmo.com**, March 27, 2007, and Parker Hannifin Corporation, online at **http://www.parker.com**, accessed June 30, 2007.

explained why his amplifier chip is so advanced that it should sell for $1.68, a third more than its rivals. His bosses' reaction: Charge even more. The chip is 20 times better than the competition, they asserted, and high-end customers will crave it on any terms. Why not boost the $1.68 list price by 10 cents? Mr. Soule was nervous. "I can live with that," he guardedly replied, "but what does that accomplish?" "It's a dime!" declared Linear's chairman and founder, Robert Swanson. "And those dimes add up."[6] The moral of the story is: If you have pricing power, use it because it doesn't last forever.

Parker Hannifin Corporation, a manufacturer of over 800,000 different parts—from heat resistant seals for jet engines to steel valves for hoist buckets—took a different approach to find pricing power. Initially, no matter how much a product improved, the company ended up charging the same markup it would for a more standard product. And if the company found a way to make a product less expensively, it ultimately cut the product's price as well. Hannifin's President, Donald Washkewica, knew that there must be a better way. He analyzed the product line searching for items that would offer pricing power. The new strategy is outlined in Exhibit 19.7. It has boosted revenue by $200 million.[7] The items identified as having greater inelasticity of demand have greater profit margins.

LO4

The Power of Yield Management Systems and Targeting Technology

yield management systems (YMS)
A technique for adjusting prices that uses complex mathematical software to profitably fill unused capacity by discounting early purchases, limiting early sales at these discounted prices, and overbooking capacity.

Another important tool for gaining pricing power is the yield management system. More and more companies are turning to yield management systems to help fine-tune prices. First developed in the airline industry, yield management systems (YMS) use complex mathematical software to profitably fill unused capacity. The software employs techniques such as discounting early purchases, limiting early sales at these discounted prices, and overbooking capacity. YMS now are appearing in other services such as lodging, other transportation forms, rental firms, retailers, and even hospitals.

Yield management systems are spreading beyond service industries as their popularity increases. The lessons of airlines and hotels aren't entirely applicable to other industries, however, because plane seats and hotel beds are perishable—if they go empty, the revenue opportunity is lost forever. So it makes sense to slash prices to move toward capacity if it's possible to do so without reducing the prices that other customers pay. Cars and steel aren't so perishable. Still, the capacity to make these goods is perishable. An underused factory or mill is a lost revenue opportunity. So it makes sense to cut prices to use up capacity if it's possible to do so while getting other customers to pay full price.

By using a type of yield management system, Allstate has gotten smarter about what to charge which drivers. In the past, customers were divided into three categories for car insurance. Now Allstate has more than 1,500 price levels. Agents used to simply refer to a manual to give customers a price; now they log on to a computer that uses complex algorithms to analyze 16 credit report variables, such as late payments and card balances, as well as data such as claims history for specific car models. Thus, safe drivers are rewarded, saving up to 20 percent over the old system, and high-risk drivers are penalized, paying up to 20 percent more. The system has worked so well that Allstate now applies it to other lines, such as homeowners' insurance.[8]

Yield management software is the reason that consumers now find prices at the 390 Longs Drug Stores in amounts like $2.07 or $5.84 instead of the traditional price-ending digits of .95 or .99. The company says the software has triggered a "category-by-category increase in sales and profit margins."[9] That's the main reason that DemandTec's YMS algorithms, and not manufacturers' suggested retail prices, now govern pricing in all Longs' stores in the continental United States.

With its lower cost structure and massive buying power, Wal-Mart has put pressure on everyone. Many retailers have fought back by slashing prices across the board—a foolhardy move, as many retailers have found out (think of Kmart). "You can't out-Wal-Mart Wal-Mart," said the CEO of Longs Drug Stores. "We'd lose that game."[10]

All the more reason, argues DemandTec's founder Michael Neal, to focus on better pricing. Neal explains that one DemandTec client, a retailer, began bargain pricing what it thought was a very price-sensitive product—diapers—to generate store traffic. But after running sales data through the pricing software, the client discovered that was not the case. Most price-conscious diaper shoppers had long since abandoned the store for bulk purchases at discounters such as Wal-Mart. As a result, the client raised prices on diapers, increasing margins without hurting sales or traffic.

TARGETING TECHNOLOGY

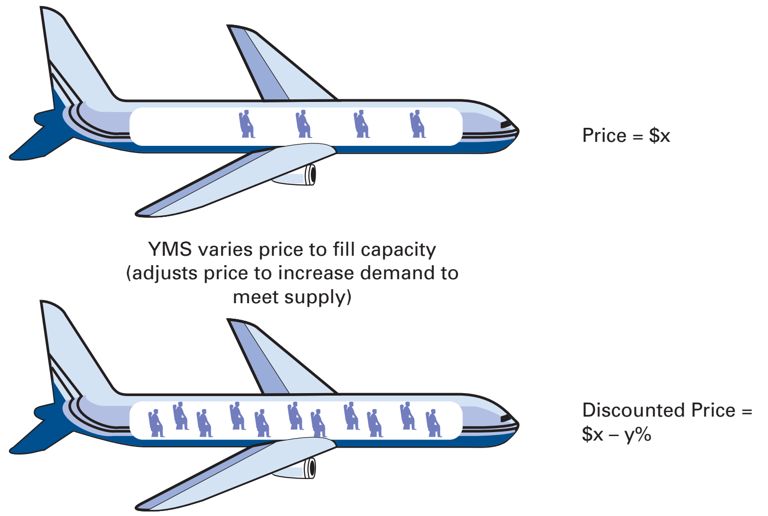
Internet retailers are now offering different prices and promotional offers to different customers based upon their Internet shopping and browsing habits. Using Internet cookies and new targeting software, Internet retailers can identify you each time you visit, and e-stores can gather reams of preferences as you shop. "It's as if we had a little camera that can watch you flip through a catalog. We can see where you stopped, what pages you dog-eared, what pages you ripped out and what made you pick up the phone to buy," says John Squire, vice president of product strategy at Coremetrics, a San Mateo, Calif. software company that helps online retailers analyze and act on consumer behavior.[11]

At Overstock.com, the company watches how long you linger on the site and how much you spend. That alone could determine whether you'll see an ad for a liquidation sale on last year's sweatshirts or a notice about a new shipment of pricey freshwater pearls. Watchmaker Fossil sometimes offers discounts and deals to first-time site visitors that it hides from repeat customers. Folks who abandon a virtual shopping cart at flower-delivery sites are sometimes e-mailed a 10 percent coupon to lure them back. Targeted offers can also boost the effectiveness of e-mail campaigns. Consumers typically open one out of five e-mail offers from retailers, and only 20 percent of those views lead to a site visit. When e-mail is customized with anything from the customer's name to a discount for something they've bought before, conversion rates double.[12]

No wonder, then, that high-profile e-commerce sites like RedEnvelope.com, Travelocity, and eBay, along with the online arms of big retailers like Circuit City, Petco, and J.C. Penney, are pouring resources into targeting technology.

REVIEW LEARNING OUTCOME

LO4 Understand the concept of yield management systems



LO5 The Cost Determinant of Price

Sometimes companies minimize or ignore the importance of demand and decide to price their products largely or solely on the basis of costs. Prices determined strictly on the basis of costs may be too high for the target market, thereby reducing or eliminating sales. On the other hand, cost-based prices may be too low, causing the firm to earn a lower return than it should. Nevertheless, costs should generally be part of any price determination, if only as a floor below which a good or service must not be priced in the long run.

The idea of cost may seem simple, but it is actually a multifaceted concept, especially for producers of goods and services. A variable cost is a cost that varies with changes in the level of output; an example of a variable cost is the cost of materials. In contrast, a fixed cost does not change as output is increased or decreased. Examples include rent and executives' salaries.

To compare the cost of production to the selling price of a product, it is helpful to calculate costs per unit, or average costs. Average variable cost (AVC) equals total variable costs divided by quantity of output. Average total cost (ATC) equals total costs divided by output. As the graph in Exhibit 19.8(a) shows, AVC and ATC are basically U-shaped curves. In contrast, average fixed cost (AFC) declines continually as output increases because total fixed costs are constant.

Marginal cost (MC) is the change in total costs associated with a one-unit change in output. Exhibit 19.8(b) shows that when output rises from seven to eight units, the change in total cost is from $640 to $750; therefore, marginal cost is $110.

All the curves illustrated in Exhibit 19.8(a) have definite relationships:

- AVC plus AFC equals ATC.
- MC falls for a while and then turns upward, in this case with the fourth unit. At that point diminishing returns set in, meaning that less output is produced for every additional dollar spent on variable input.
- MC intersects both AVC and ATC at their lowest possible points.
- When MC is less than AVC or ATC, the incremental cost will continue to pull the averages down. Conversely, when MC is greater than AVC or ATC, it pulls the averages up, and ATC and AVC begin to rise.
- The minimum point on the ATC curve is the least cost point for a fixed-capacity firm, although it is not necessarily the most profitable point.

Costs can be used to set prices in a variety of ways. For example, markup pricing is relatively simple. Profit maximization pricing and break-even pricing make use of the more complicated concepts of cost.

One company that is maniacal about controlling costs is Ryanair, as explained in the Global Perspectives box in this chapter.

variable cost
A cost that varies with changes in the level of output.

fixed cost
A cost that does not change as output is increased or decreased.

average variable cost (AVC)
Total variable costs divided by quantity of output.

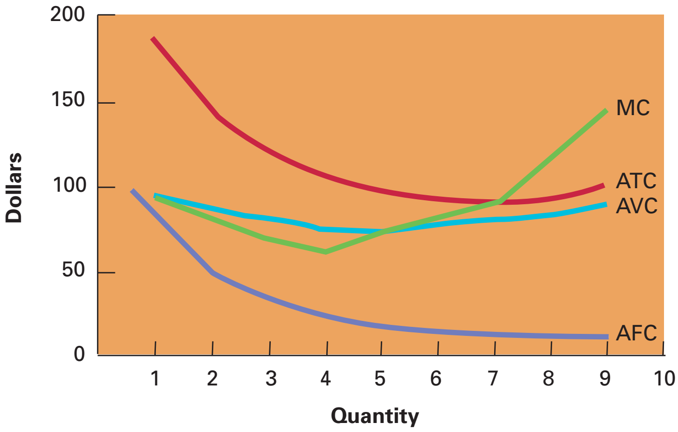
average total cost (ATC)
Total costs divided by quantity of output.

marginal cost (MC)
The change in total costs associated with a one-unit change in output.

Exhibit 19.8

Hypothetical Set of Cost Curves and a Cost Schedule

(a) Cost curves



(b) Cost schedule

Total-cost data, per week				Average-cost data, per week			
(1) Total product (Q)	(2) Total fixed cost (TFC)	(3) Total variable cost (TVC)	(4) Total cost (TC)	(5) Average fixed cost (AFC)	(6) Average variable cost (AVC)	(7) Average total cost (ATC)	(8) Marginal cost (MC)
			TC = TFC + TVC	$AFC = \frac{TFC}{Q}$	$AVC = \frac{TVC}{Q}$	$ATC = \frac{TC}{Q}$	$(MC) = \frac{\text{change in TC}}{\text{change in Q}}$
0	$100	$ 0	$ 100	—	—	—	—
1	100	90	190	$100.00	$90.00	$190.00	$ 90
2	100	170	270	50.00	85.00	135.00	80
3	100	240	340	33.33	80.00	113.33	70
4	100	300	400	25.00	75.00	100.00	60
5	100	370	470	20.00	74.00	94.00	70
6	100	450	550	16.67	75.00	91.67	80
7	100	540	640	14.29	77.14	91.43	90
8	100	650	750	12.50	81.25	93.75	110
9	100	780	880	11.11	86.67	97.78	130
10	100	930	1,030	10.00	93.00	103.00	150

MARKUP PRICING

Markup pricing, the most popular method used by wholesalers and retailers to establish a selling price, does not directly analyze the costs of production. Instead, markup pricing uses the cost of buying the product from the producer, plus amounts for profit and for expenses not otherwise accounted for. The total determines the selling price.

markup pricing
The retail price of a product determined by adding the cost from the producer plus amounts for profit and for expenses not otherwise accounted for.

A retailer, for example, adds a certain percentage to the cost of the merchandise received to arrive at the retail price. An item that costs the retailer $1.80 and is sold for $2.20 carries a markup of 40 cents, which is a markup of 22 percent on the cost ($.40 ÷ $1.80). Retailers tend to discuss markup in terms of its percentage of the retail price—in this example, 18 percent ($.40 ÷ $2.20). The difference

GLOBAL Perspectives

Make More Money by Letting Them Fly Free

Michael O'Leary, Chief Executive of Ireland's Ryanair, Europe's most profitable airline, wants to make air travel free. Not free as in free from regulation, but free as in zero cost. By the end of 2010, he promises, "more than half of our passengers will fly free." The remarkable thing is, few analysts think his prediction is far-fetched: Ryanair already offers free fares to a quarter of its customers.

Even without free flights, Ryanair has become one of Europe's most popular carriers. Each year it flies over 35 million passengers to more than 100 European destinations, while its customers pay an average fare of just $53. Even more impressive, Ryanair's 22 percent net profit margin leads the industry. (By comparison, Southwest Airline's net margin is 7.2 percent.)

The secret? Ryanair's austere cost structure almost makes Southwest look extravagant. In addition, the Irish airline puts a price on virtually everything *except* tickets, from baggage check-in to seat-back advertising space. As a result, recently Ryanair collected $265 million—15.6 percent of overall revenues—from sources other than ticket sales.

Like Wal-Mart, each time Ryanair comes up with a new way to cut costs by a few million dollars—for example, by removing seat-back pockets to reduce weight and cleaning expense—O'Leary passes the savings along to customers in the form of lower fares. It also means charging passengers for practically every amenity they might consume. There are no free peanuts or beverages on Ryanair flights; 27 million passengers bought in-flight refreshments on the airline in 2007, generating sales of $61 million, or an average of $2.25 per person. Ryanair has eliminated its free checked-bag allowance and began charging $3.50 per piece—a "revenue-neutral" fee that was offset by cutting ticket prices by an average of $3.50. Ryanair expects the move to save $36 million a year by reducing fuel and handling costs.

The airline is just as aggressive in its efforts to develop new sources of revenue. Today, 98 percent of Ryanair's passengers book their flights online, and the company's website sees roughly 15 million unique visitors a month—making it Europe's most popular travel site. The airline uses that traffic as a marketing tool for related services; each time a passenger books a rental car or a hotel room, Ryanair earns a percentage of the sale.

O'Leary is also starting to turn his planes into media and entertainment plays. He's offered advertisers the opportunity to repaint the exteriors of Ryanair's planes, effectively turning them into giant billboards. (Hertz, Jaguar, and Vodafone have purchased space on the fuselages of Ryanair's 737s.) For passengers seeking distraction, Ryanair intends to offer in-flight gambling, with the airline earning a tiny cut off of each wager. O'Leary thinks gambling could double Ryanair's profits over the next decade.[13]

Do you think that Ryanair is overly obsessed with cost cutting? Isn't it lowering service quality? Would the Ryanair approach be successful in the United States? If a customer pays extra for everything but the ticket, isn't the cost about the same as a regular priced ticket?

SOURCE: From Malhew Maier, "A Radical Fix for Airlines: Make Flying Free", 'Business 2.0', April 2006, pp. 32-34.

between the retailer's cost and the selling price (40 cents) is the gross margin, as Chapter 15 explained.

PR NEWSFOTO/© NINTENDO

It is not uncommon for specialty retailers to mark up their merchandise by 100 percent, even more in industries like popular video gaming equipment.

$$\text{Retail price} = \frac{\text{Cost}}{1 - \text{Desired return on sales}}$$

$$= \frac{\$1.80}{1.00 - .18}$$

$$= \$2.20$$

If the retailer wants a 30 percent return, then:

$$\text{Retail price} = \frac{\$1.80}{1.00 - .30}$$

$$= \$2.57$$

The reason that retailers and others speak of markups on selling price is that many important figures in financial reports, such as gross sales and revenues, are sales figures, not cost figures.

To use markup based on cost or selling price effectively, the marketing manager must calculate an adequate gross margin—the amount added to cost to determine price. The margin must ultimately provide adequate funds to cover selling expenses and profit. Once an appropriate margin has been determined, the markup technique has the major advantage of being easy to employ. Wal-Mart, for example, strives for a gross margin of around 16 percent. Because supermarket chains, such as Safeway and Kroger, have typically had gross margins of 24 percent, they are now finding it extremely difficult to compete with Wal-Mart supermarkets. Wal-Mart is now the nation's largest grocery chain.

Markups are often based on experience. For example, many small retailers mark up merchandise 100 percent over cost. (In other words, they double the cost.) This tactic is called keystoning. Some other factors that influence markups are the merchandise's appeal to customers, past response to the markup (an implicit demand consideration), the item's promotional value, the seasonality of the goods, their fashion appeal, the product's traditional selling price, and competition. Most retailers avoid any set markup because of such considerations as promotional value and seasonality.

keystoning
The practice of marking up prices by 100 percent, or doubling the cost.

profit maximization
A method of setting prices that occurs when marginal revenue equals marginal cost.

marginal revenue (MR)
The extra revenue associated with selling an extra unit of output or the change in total revenue with a one-unit change in output.

break-even analysis
A method of determining what sales volume must be reached before total revenue equals total costs.

PROFIT MAXIMIZATION PRICING

Producers tend to use more complicated methods of setting prices than distributors use. One is profit maximization, which occurs when marginal revenue equals marginal cost. You learned earlier that marginal cost is the change in total costs associated with a one-unit change in output. Similarly, marginal revenue (MR) is the extra revenue associated with selling an extra unit of output. As long as the revenue of the last unit produced and sold is greater than the cost of the last unit produced and sold, the firm should continue manufacturing and selling the product.

Exhibit 19.9 shows the marginal revenues and marginal costs for a hypothetical firm, using the cost data from Exhibit 19.8(b). The profit-maximizing quantity, where MR = MC, is six units. You might say, "If profit is zero, why produce the sixth unit? Why not stop at five?" In fact, you would be right. The firm, however, would not know that the fifth unit would produce zero profits until it determined that profits were no longer increasing. Economists suggest producing up to the point where MR = MC. If marginal revenue is just one penny greater than marginal costs, it will still increase total profits.

Exhibit 19.9

Point of Profit Maximization

Quantity	Marginal Revenue (MR)	Marginal Cost (MC)	Cumulative Total Profit
0	—	—	—
1	$140	$90	$50
2	130	80	100
3	105	70	135
4	95	60	170
5	85	70	185
*6	80	80	185
7	75	90	170
8	60	110	120
9	50	130	40
10	40	150	(70)

*Profit maximization.

BREAK-EVEN PRICING

Now let's take a closer look at the relationship between sales and cost. Break-even analysis determines what sales volume must be reached before the company breaks even (its total costs equal total revenue) and no profits are earned. Managers want to know how much they must sell before the firm starts earning a profit.

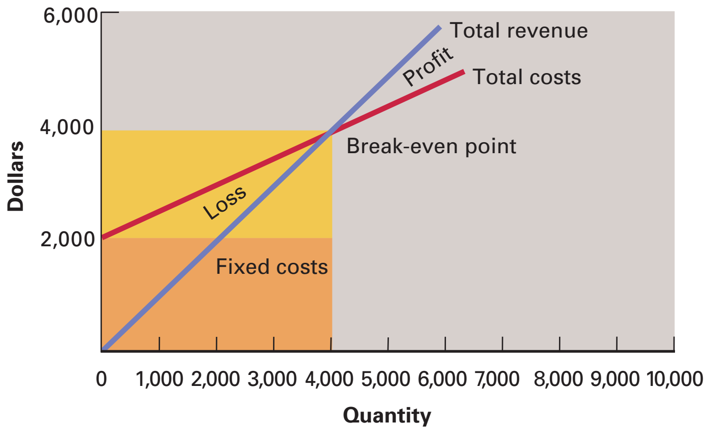
The typical break-even model assumes a given fixed cost and a constant average variable cost. Suppose that Universal Sportswear, a hypothetical firm, has fixed costs of $2,000 and that the cost of labor and materials for each unit produced is 50 cents. Assume that it can sell up to 6,000 units of its product at $1 without having to lower its price.

Exhibit 19.10(a) illustrates Universal Sportswear's break-even point. As Exhibit 19.10(b) indicates, Universal Sportswear's total variable costs increase by 50 cents every time a new unit is produced, and total fixed costs remain constant at $2,000 regardless of the level of output. Therefore, for 4,000 units of output, Universal Sportswear has $2,000 in fixed costs and $2,000 in total variable costs (4,000 units × $.50), or $4,000 in total costs.

Exhibit 19.10

Costs, Revenues, and Break-Even Point for Universal Sportswear

(a) Break-even point



(b) Costs and revenues

Output	Total fixed costs	Average variable costs	Total variable costs	Average total costs	Average revenue (price)	Total revenue	Total costs	Profit or loss
500	$2,000	$0.50	$ 250	$4.50	$1.00	$ 500	$2,250	($1,750)
1,000	2,000	0.50	500	2.50	1.00	1,000	2,500	(1,500)
1,500	2,000	0.50	750	1.83	1.00	1,500	2,750	(1,250)
2,000	2,000	0.50	1,000	1.50	1.00	2,000	3,000	(1,000)
2,500	2,000	0.50	1,250	1.30	1.00	2,500	3,250	(750)
3,000	2,000	0.50	1,500	1.17	1.00	3,000	3,500	(500)
3,500	2,000	0.50	1,750	1.07	1.00	3,500	3,750	(250)
*4,000	2,000	0.50	2,000	1.00	1.00	4,000	4,000	0
4,500	2,000	0.50	2,250	.94	1.00	4,500	4,250	250
5,000	2,000	0.50	2,500	.90	1.00	5,000	4,500	500
5,500	2,000	0.50	2,750	.86	1.00	5,500	4,750	750
6,000	2,000	0.50	3,000	.83	1.00	6,000	5,000	1,000

*Break-even point

Revenue is also $4,000 (4,000 units × $1), giving a net profit of zero dollars at the break-even point of 4,000 units. Notice that once the firm gets past the break-even point, the gap between total revenue and total costs gets wider and wider because both functions are assumed to be linear.

The formula for calculating break-even quantities is simple:

$$\text{Break-even quantity} = \frac{\text{Total fixed costs}}{\text{Fixed cost contribution}}$$

Fixed cost contribution is the price minus the average variable cost. Therefore, for Universal Sportswear,

$$\text{Break-even quantity} = \frac{\$2{,}000}{(\$1.00 - \$.50)}$$

$$= \frac{\$2{,}000}{\$.50}$$

$$= 4{,}000 \text{ units}$$

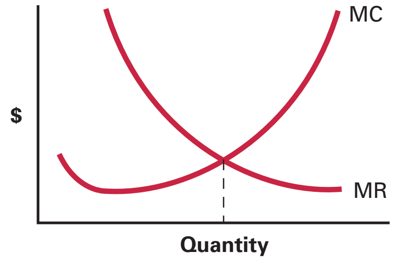
The advantage of break-even analysis is that it provides a quick estimate of how much the firm must sell to break even and how much profit can be earned if a higher sales

REVIEW LEARNING OUTCOME

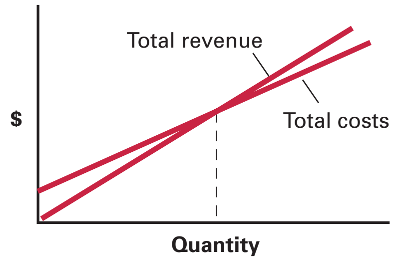
LO 5 Describe cost-oriented pricing strategies

Markup: Cost + x% = Price

Profit Maximization: Price set at point where MR = MC



Break-even: Price set at point where total cost = total revenue



volume is obtained. If a firm is operating close to the break-even point, it may want to see what can be done to reduce costs or increase sales. Moreover, in a simple break-even analysis, it is not necessary to compute marginal costs and marginal revenues because price and average cost per unit are assumed to be constant. Also, because accounting data for marginal cost and revenue are frequently unavailable, it is convenient not to have to depend on that information.

Break-even analysis is not without several important limitations. Sometimes it is hard to know whether a cost is fixed or variable. If labor wins a tough guaranteed-employment contract, are the resulting expenses a fixed cost? Are middle-level executives' salaries fixed costs? More important than cost determination is the fact that simple break-even analysis ignores demand. How does Universal Sportswear know it can sell 4,000 units at $1? Could it sell the same 4,000 units at $2 or even $5? Obviously, this information would profoundly affect the firm's pricing decisions.

LO 6 Other Determinants of Price

Other factors besides demand and costs can influence price. For example, the stages in the product life cycle, the competition, the product distribution strategy, the promotion strategy, and perceived quality can all affect pricing.

STAGES IN THE PRODUCT LIFE CYCLE

As a product moves through its life cycle (see Chapter 10), the demand for the product and the competitive conditions tend to change:

- *Introductory stage:* Management usually sets prices high during the introductory stage. One reason is that it hopes to recover its development costs quickly. In addition, demand originates in the core of the market (the customers whose needs ideally match the product's attributes) and thus is relatively inelastic. On the other hand, if the target market is highly price sensitive, management often finds it better to price the product at the market level or lower. For example, when Kraft Foods brought out Country Time lemonade, it was priced like similar products in the highly competitive beverage market because the market was price sensitive.
- *Growth stage:* As the product enters the growth stage, prices generally begin to stabilize for several reasons. First, competitors have entered the market, increasing the available supply. Second, the product has begun to appeal to a broader market, often lower-income groups. Finally, economies of scale are lowering costs, and the savings can be passed on to the consumer in the form of lower prices.

Competition often affects pricing strategies. This 1and1 advertisement compares the company's prices to its competitors', proving that 1and1 is the most affordable Web host available.

- *Maturity stage:* Maturity usually brings further price decreases as competition increases and inefficient, high-cost firms are eliminated. Distribution channels become a significant cost factor, however, because of the need to offer wide product lines for highly segmented markets, extensive service requirements, and the sheer number of dealers necessary to absorb high-volume production. The manufacturers that remain in the market toward the end of the maturity stage typically offer similar prices. Usually, only the most efficient remain, and they have comparable costs. At this stage, price increases are usually cost initiated, not demand initiated. Nor do price reductions in the late phase of maturity stimulate much demand. Because demand is limited and producers have similar cost structures, the remaining competitors will probably match price reductions.
- *Decline stage:* The final stage of the life cycle may see further price decreases as the few remaining competitors try to salvage the last vestiges of demand. When only one firm is left in the market, prices begin to stabilize. In fact, prices may eventually rise dramatically if the product survives and moves into the specialty goods category, as horse-drawn carriages and vinyl records have.

THE COMPETITION

Competition varies during the product life cycle, of course, and so at times it may strongly affect pricing decisions. Although a firm may not have any competition at first, the high prices it charges may eventually induce another firm to enter the market. A number of Internet auto sellers, such as Autobytel.com, have sprung up in response to the perceived high profit margins earned by car dealers.

On the other hand, intense competition can sometimes lead to price wars. One company recently took action to avoid a calamitous price war by outsmarting its competition. A company (call it Acme) heard that its competitor was trying to steal some business by offering a low price to one of its best customers. Instead of immediately cutting prices, Acme reps visited three of its competitor's best clients and said they figured the client was paying x, the same price that the competitor had quoted to Acme's own customer. Within days, the competitor had retracted its low-price offer to Acme's client. Presumably, the competitor had received calls from three angry clients asking for the same special deal.

selling against the brand
Stocking well-known branded items at high prices in order to sell store brands at discounted prices.

© AP PHOTO/YVES LOGGHE

European Union Commissioner for Justice, Freedom and Security, Franco Frattini looks at counterfeit products displayed on a table at the EU Commission headquarters in Brussels. The European Commission has proposed minimum four-year jail terms as part of a new beefed up European Union law to fight counterfeiters and piracy.

DISTRIBUTION STRATEGY

An effective distribution network can often overcome other minor flaws in the marketing mix.[14] For example, although consumers may perceive a price as being slightly higher than normal, they may buy the product anyway if it is being sold at a convenient retail outlet.

Adequate distribution for a new product can often be attained by offering a larger-than-usual profit margin to distributors. A variation on this strategy is to give dealers a large trade allowance to help offset the costs of promotion and further stimulate demand at the retail level.

Manufacturers have gradually been losing control within the distribution channel to wholesalers and retailers, which often adopt pricing strategies that serve their own purposes. For instance, some distributors are **selling against the brand:** They place well-known brands on the shelves at high prices while offering other brands—typically, their private-label brands, such as Craftsman tools, Kroger canned pears, or Cost Cutter paper towels—at lower prices. Of course, sales of the higher-priced brands decline.

Wholesalers and retailers may also go outside traditional distribution channels to buy gray-market goods. As explained previously, distributors obtain the goods through unauthorized channels for less than they would normally pay, so they can sell the goods with a bigger-than-normal markup or at a reduced price. Imports seem to be particularly susceptible to gray marketing. Porsches, JVC stereos, and Seiko watches are among the brand-name products that have experienced this problem. Although consumers may pay less for gray-market goods, they often find that the manufacturer won't honor the warranty.

Manufacturers can regain some control over price by using an exclusive distribution system, by franchising, or by avoiding doing business with price-cutting discounters. Manufacturers can also package merchandise with the selling price marked on it or place goods on consignment. The best way for manufacturers to control prices, however, is to develop brand loyalty in consumers by delivering quality and value.

THE IMPACT OF THE INTERNET

The Internet, corporate networks, and wireless setups are linking people, machines, and companies around the globe—and connecting sellers and buyers as never before. This link is enabling buyers to quickly and easily compare products and prices, putting them in a better bargaining position. At the same time, the technology allows sellers to collect detailed data about customers' buying habits, preferences, and even spending limits so that the sellers can tailor their products and prices.

Picking a Product to Buy Online

The online shopping process begins with selecting a product. If you want a pet, camera, electronics product, or computer but don't know which brand, try **http://www.activebuyersguide.com,** which will help you narrow your choice. If you want help with outdoor gear, try **http://outside.away.com.** Once you select a brand, you can always get a second opinion at **http://www.consumersearch.com**. This is an expert site that aggregates reviews from many sources such as Consumer Digest, Consumer Reports, and PC World. For example, a quick click on sleeping bags led to reviews from *Backpacker* and *Outside* magazines. The problem with expert reviews is that each judgment reflects the views of a few people at most. Many shoppers find **http://www.consumerreview.com** or **http://www.epinions.com** helpful. These sites provide user opinions of hundreds of different products. Unfortunately, consumer reviews vary widely in quality. Some are quite terse whereas others tend to ramble on and on.

Using Shopping Bots

A shopping bot is a program that searches the Web for the best price for a particular item that you wish to purchase. Bot is short for robot. Shopping bots theoretically give pricing power to the consumer. The more information that the shopper has, the more efficient his or her purchase decision will be. When consumers use their money wisely, they can raise their standard of living by approximately one-third. This applies not only to purchasing but to the wise use of credit as well.

There are two general types of shopping bots. The first is the broad-based type that searches a wide range of product categories such as MySimon.com, dealtime.com, bizmate.com, pricegrabber.com, and PriceScan.com. These sites operate using a Yellow Pages type of model, in that they list every retailer they can find. The second is the niche-oriented type that searches for only one type of product such as computer equipment (CNET.com), books (Bookfinder.com), or CDs (CDPriceCompare.com).

Most shopping bots give preferential listings to those e-retailers that pay for the privilege. These so-called merchant partners receive about 60 percent of the click-throughs.[15] Typically, the bot lists its merchant partners first, not the retailer that offers the lowest price.

If a bot steers you to really low prices, be careful, as Internet fraud is huge. If you are considering buying from a site that you don't know, check out customer feedback at **http://www.resellerratings.com or http://ratingwonders.com**. Also, if a merchant's site doesn't answer questions about the product, call for details before giving out your credit-card information. Sometimes a really low price is for a reconditioned or refurbished item, or, in the case of clothing and similar items, it may be a "second." Also, ask about in-stock status, pricing breakdowns such as taxes and shipping, and return policies including restocking charges.

In summary, recent research on 1500 car purchases found that consumers who used the Internet received about a two percent lower price. The Internet lowers prices for two distinct reasons: First, the Internet informs consumers. The information that seems to be most valuable to consumers in the auto study was the invoice price of the dealer; it enables them to negotiate a low price at a given dealership. Internet information seems not to help consumers find low-price dealerships. In particular, the Internet does not substitute for searching at multiple dealers, and searching at multiple dealers does not substitute for being better informed.

Second, the incentives provided by online buying services' contracts with dealerships help consumers obtain lower prices through a referral process. Referrals from manufacturer Web sites do not lower prices. Online buying services, such as autobytel.com or edmunds.com, are more effective because unlike manufacturers, they can exert pressure on dealers by directing incremental business to affiliated (and away from unaffiliated) dealerships.[16]

Internet Auctions

The Internet auction business is huge. Part of the lure of buying online is that shoppers don't have to go to a flea market or use up a coveted weekend day or worry about the weather. Plus, bidding itself can be fun and exciting. Among the most popular consumer auction sites are the following:

- **http://www.auctions.amazon.com:** Links to Sotheby's for qualified sellers of high-end items.
- **http://www.ebay.com:** The most popular auction site.
- **http://bidz.com/:** Bidz.com buys closeout deals in very large lots and offers them online in their no-reserve auctions.

Even though consumers are spending billions on Internet auctions, business-to-business (B2B) auctions are likely to be the dominant form in the future. Recently, Whirlpool began holding online auctions. Participants bid on the price of the items that they would supply to Whirlpool, but with a twist: they had to include the date when Whirlpool would have to pay for the items. The company wanted to see which suppliers would offer the longest grace period before requiring payment. Five auctions held over five months helped Whirlpool uncover savings of close to $2 million and more than doubled the grace period.

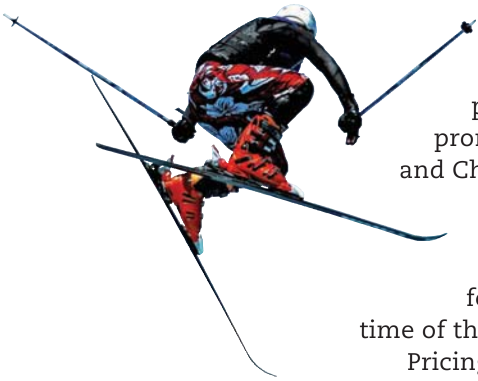
Whirlpool's success is a sign that the B2B auction world is shifting from haggling over prices to niggling over parameters of the deal. Warranties, delivery dates, transportation methods, customer support, financing options, and quality have all become bargaining chips.

There is also a dark side to Internet auctions, however, especially those where most participants are consumers. Every day crooks lure hundreds of unsuspecting users with auctions that appear legitimate but are really a hollow shell. They hop from user ID to user ID, feeding the system with fake information and stolen credit cards so that the auction site can't tell who they are. In response to a dramatic increase in auction-fraud complaints, the Federal Trade Commission banded together with the National Association of Attorneys General to conduct Operation Bidder Beware, a nationwide crackdown and consumer-education campaign.

Consumers lost $198.4 million in 2006 to online fraud. The FBI Internet Crime Complaint Center reported that 207,492 complaints of online crime were filed and 63 percent of these involved auction fraud. The most common complaint (45 percent) involved delivery of something other than what was ordered; 19 percent concerned undelivered merchandise or unpaid bills.[17]

Although the majority of transactions on eBay come off without a hitch, fraud may be more prevalent than the company lets on. The company reports that only 0.01 percent of all completed auctions are fraudulent, but the numbers don't include everyone who's been a victim of fraud.[18] They're based on the people who go through eBay's fraud-insurance claim process and thus don't include victims who for whatever reason fail to complete the process or don't start it in the first place because they don't see the point of applying for the maximum $175 reimbursement when they've lost, say, $3,000.

PROMOTION STRATEGY



Price is often used as a promotional tool to increase consumer interest. The weekly flyers sent out by grocery stores in the Sunday newspaper, for instance, advertise many products with special low prices. Crested Butte Ski Resort in Colorado tried a unique twist on price promotions. It made the unusual offer of free skiing between Thanksgiving and Christmas. Its only revenues were voluntary contributions from lodging and restaurant owners who benefited from the droves of skiers taking advantage of the promotion. Lodging during the slack period is now booked solid, and on the busiest days 9,000 skiers jam slopes designed for about 6,500. Crested Butte Resort no longer loses money during this time of the year.

Pricing can be a tool for trade promotions as well. For example, Levi's Dockers (casual men's pants) are very popular with white-collar men ages 25 to 45, a growing and lucrative market. Sensing an opportunity, rival pants-maker Bugle Boy began offering similar pants at cheaper wholesale prices, which gave retailers a bigger gross margin than they were getting with Dockers. Levi Strauss had to either lower prices or risk its $400 million annual Dockers sales. Although Levi Strauss intended its cheapest Dockers to retail for $35, it started selling Dockers to retailers for $18 a pair. Retailers could then advertise Dockers at a very attractive retail price of $25.

GUARANTEED PRICE MATCHING

Closely related to promotion pricing is the price guarantee. In its most basic form, a firm promotes the fact that it will match any competitor's price. Others, such as Hotwire.com, claim that they will refund double the difference if you find a lower airfare or hotel price. One of your authors recently booked a hotel on Hotwire and subsequently found a lower rate through Mobissimo.com. Mobissimo is a Web crawler that searches over 175 sites and then passes you directly to the site that you select. After finding the cheaper rate, Hotwire credited his account for $160! It was double the difference in prices!! On the downside, the same author booked a car on Hotwire for a week for $265. He had to cancel the trip and Hotwire kept his $265 because of its "no cancellation" policy.

Research shows that when a retailer offers a price-matching guarantee, it is signaling to the target market that it is positioned as a low-price dealer. Conversely, a lack of a price-matching guarantee signals a high-service positioning.[19]

DEMANDS OF LARGE CUSTOMERS

Manufacturers find that their large customers such as Wal-Mart, JCPenney, and other department stores often make specific pricing demands that the suppliers must agree to. Department stores are making greater-than-ever demands on their suppliers to cover the heavy discounts and markdowns on their own selling floors. They want suppliers to guarantee their stores' profit margins, and they insist on cash rebates if the guarantee isn't met. They are also exacting fines for violations of ticketing, packing, and shipping rules. Cumulatively, the demands are nearly wiping out profits for all but the very biggest suppliers, according to fashion designers and garment makers.

With annual sales of over $375 billion and 1.9 million "associates" (employees), Wal-Mart is the world's largest company. Wal-Mart is the largest customer of Disney brands, Procter & Gamble, Kraft, Gillette, Campbell Soups, and most of America's other leading branded manufacturers. Wal-Mart expects suppliers to offer their best price, period. There is no negotiation or raising prices later. When suppliers have raised prices, Wal-Mart has been known to keep sending the old amount.[20]

THE RELATIONSHIP OF PRICE TO QUALITY

prestige pricing
Charging a high price to help promote a high-quality image.

When a purchase decision involves great uncertainty, consumers tend to rely on a high price as a predictor of good quality. Reliance on price as an indicator of quality seems to occur for all products, but it reveals itself more strongly for some items than for others.[21] Among the products that benefit from this phenomenon are coffee, stockings, aspirin, salt, floor wax, shampoo, clothing, furniture, perfume, whiskey, and many services. In the absence of other information, people typically assume that prices are higher because the products contain better materials, because they are made more carefully, or, in the case of professional services, because the provider has more expertise. In other words, consumers assume that "You get what you pay for."

Research has found that products that are perceived to be of high quality tend to benefit more from price promotions than products perceived to be of lower quality.[22] However, when perceived high- and lower-quality products are offered in settings where consumers have difficulty making comparisons, then price promotions have an equal effect on sales. Comparisons are more difficult in end-of-aisle displays, feature advertising, and the like.

Knowledgeable merchants take these consumer attitudes into account when devising their pricing strategies. Prestige pricing is charging a high price to help promote a high-quality

REVIEW LEARNING OUTCOME

LO 1 Demonstrate how the product life cycle, competition, distribution and promotion strategies, customer demands, the Internet, and perceptions of quality can affect pricea

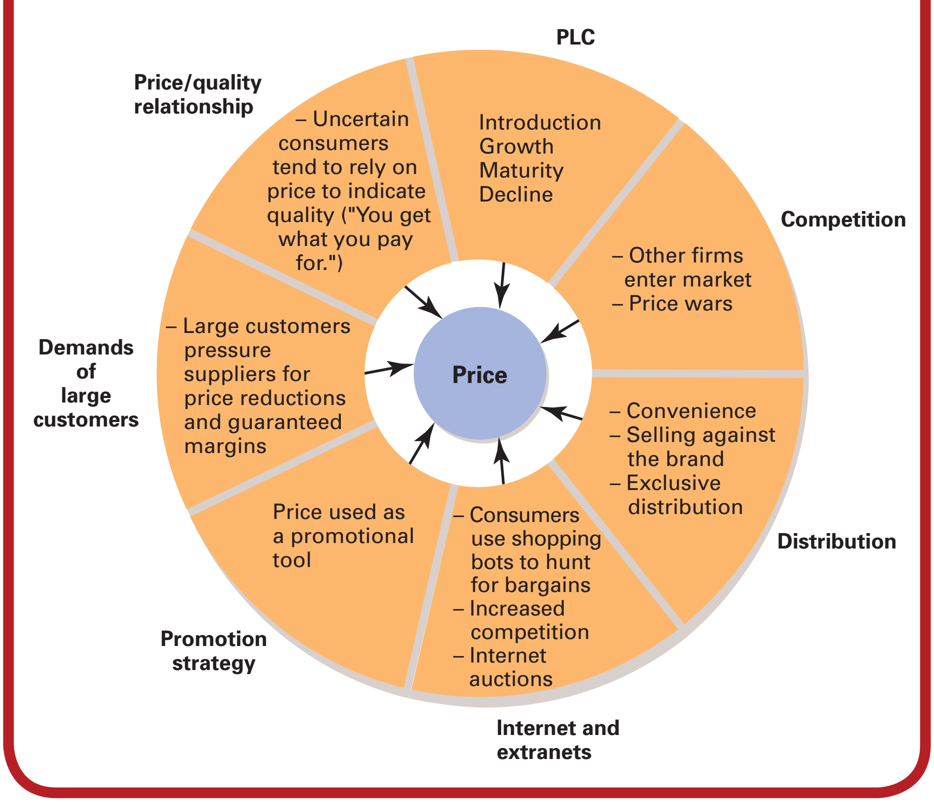


image. A successful prestige pricing strategy requires a retail price that is reasonably consistent with consumers' expectations. No one goes shopping at a Gucci's shop in New York and expects to pay $9.95 for a pair of loafers. In fact, demand would fall drastically at such a low price. Bayer aspirin would probably lose market share over the long run if it lowered its prices. A new mustard packaged in a crockery jar was not successful until its price was doubled.

Some of the latest research on price-quality relationships has focused on consumer durable goods. The researchers first conducted a study to ascertain the dimensions of quality. These are (1) ease of use; (2) versatility (the ability of a product to perform more functions, e.g., special stitch types on sewing machines, or be more flexible, e.g., continuous temperature controls on microwave ovens); (3) durability; (4) serviceability (ease of obtaining quality repairs); (5) performance; and (6) prestige. The researchers found that when consumers focused on prestige and/or durability to assess quality, price was a strong indicator of perceived overall quality. Price was less important as an indicator of quality if the consumer was focusing on one of the other four dimensions of quality.[23]

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a satisfactory profit in a high-risk industry > **35%**

8,000 < jobs slashed by Freightliner to cut costs

used cars inspected annually in Nevada > **400,000**

price of a Rolling Stones concert ticket > **$400**

1,500 < price levels at Allstate

price decrease for safe drivers and increase for unsafe drivers > **20%**

Ryanair's percent profit margin > **22**

100% < price markup used by small-retailers

Review And Applications

LO 1 **Discuss the importance of pricing decisions to the economy and to the individual firm.** Pricing plays an integral role in the U.S. economy by allocating goods and services among consumers, governments, and businesses. Pricing is essential in business because it creates revenue, which is the basis of all business activity. In setting prices, marketing managers strive to find a level high enough to produce a satisfactory profit.

1.1 Why is pricing so important to the marketing manager?

1.2 How does price allocate goods and services?

LO 2 **List and explain a variety of pricing objectives.** Establishing realistic and measurable pricing objectives is a critical part of any firm's marketing strategy. Pricing objectives are commonly classified into three categories: profit oriented, sales oriented, and status quo. Profit-oriented pricing is based on profit maximization, a satisfactory level of profit, or a target return on investment. The goal of profit maximization is to generate as much revenue as possible in relation to cost. Often, a more practical approach than profit maximization is setting prices to produce profits that will satisfy management and stockholders. The most common profit-oriented strategy is pricing for a specific return on investment relative to a firm's assets. The second type of pricing objective is sales oriented, and it focuses on either maintaining a percentage share of the market or maximizing dollar or unit sales. The third type of pricing objective aims to maintain the status quo by matching competitors' prices.

2.1 Give an example of each major type of pricing objective.

2.2 Why do many firms not maximize profits?

LO3 **Explain the role of demand in price determination.** Demand is a key determinant of price. When establishing prices, a firm must first determine demand for its product. A typical demand schedule shows an inverse relationship between quantity demanded and price: When price is lowered, sales increase; and when price is increased, the quantity demanded falls. For prestige products, however, there may be a direct relationship between demand and price: the quantity demanded will increase as price increases.

Marketing managers must also consider demand elasticity when setting prices. Elasticity of demand is the degree to which the quantity demanded fluctuates with changes in price. If consumers are sensitive to changes in price, demand is elastic; if they are insensitive to price changes, demand is inelastic. Thus, an increase in price will result in lower sales for an elastic product and little or no loss in sales for an inelastic product. Inelastic demand creates pricing power.

3.1 Explain the role of supply and demand in determining price.

3.2 If a firm can increase its total revenue by raising its price, shouldn't it do so?

3.3 Explain the concepts of elastic and inelastic demand. Why should managers understand these concepts?

LO4 **Understand the concept of yield management systems and targeting technology.** Yield management systems use complex mathematical software to profitably fill unused capacity. The software uses techniques such as discounting early purchases, limiting early sales at these discounted prices, and overbooking capacity. These systems are used in service and retail businesses and are substantially raising revenues. The use of Internet cookies and targeting software enables online retailers to offer different pricing and promotional offers to online buyers based upon their online shopping and browsing habits.

4.1 Why are so many companies adopting yield management systems?

4.2 Explain the relationship between supply and demand and yield management systems.

4.3 Why is targeting technology so effective?

LO5 **Describe cost-oriented pricing strategies.** The other major determinant of price is cost. Marketers use several cost-oriented pricing strategies. To cover their own expenses and obtain a profit, wholesalers and retailers commonly use markup pricing: They tack an extra amount onto the manufacturer's original price to cover their costs and earn a profit. Another pricing technique is to maximize profits by setting price where marginal revenue equals marginal cost. Still another pricing strategy determines how much a firm must sell to break even and uses this amount as a reference point for adjusting price.

WRITING

5.1 Your firm has based its pricing strictly on cost in the past. As the newly hired marketing manager, you believe this policy should change. Write the president a memo explaining your reasons.

5.2 Why is it important for managers to understand the concept of break-even points? Are there any drawbacks?

LO6 **Demonstrate how the product life cycle, competition, distribution and promotion strategies, guaranteed price matching, customer demands, the Internet, and perceptions of quality can affect price.** The price of a product normally changes as it moves through the life cycle and as demand for the product and competitive conditions change. Management often sets a high price at the introductory stage, and the high price tends to attract competition. The competition usually drives prices down because individual competitors lower prices to gain market share.

Adequate distribution for a new product can sometimes be obtained by offering a larger-than-usual profit margin to wholesalers and retailers. The Internet enables consumers to compare products and prices quickly and efficiently. Price is also used as a promotional tool to attract customers. Special low prices often attract new customers and entice existing customers to buy more. Price matching positions the retailer as a low price vendor. Firms that don't match prices are perceived as offering a higher level of service. Large buyers can extract price concessions from vendors. Such demands can squeeze the profit margins of suppliers.

Perceptions of quality can also influence pricing strategies. A firm trying to project a prestigious image often charges a premium price for a product. Consumers tend to equate high prices with high quality.

6.1 Divide the class into teams of five. Each team will be assigned a different grocery store from a different chain. (An independent is fine.) Appoint a group leader. The group leaders should meet as a group and pick 15 nationally branded grocery items. Each item should be specifically described as to brand name and size of the package. Each team will then proceed to its assigned store and collect price data on the 15 items. The team should also gather price data on 15 similar store brands and 15 generics, if possible.

Each team should present its results to the class and discuss why there are price variations between stores, national brands, store brands, and generics.

As a next step, go back to your assigned store and share the overall results with the store manager. Bring back the manager's comments and share them with the class.

6.2 How does the stage of a product's life cycle affect price? Give some examples.

6.3 Go to Priceline.com (**http://www.priceline.com**). Can you research a ticket's price before purchasing it? What products and services are available for purchasing? How comfortable are you with naming your own price? Relate the supply and demand curves to customer-determined pricing.

Key Terms

average total cost (ATC)	580	marginal cost (MC)	580	return on investment (ROI)	570
average variable cost (AVC)	580	marginal revenue (MR)	583	revenue	568
break-even analysis	583	market share	571	selling against the brand	586
demand	573	markup pricing	581	status quo pricing	572
elastic demand	574	prestige pricing	590	supply	573
elasticity of demand	574	price	568	unitary elasticity	575
fixed cost	580	price equilibrium	574	variable cost	580
inelastic demand	574	profit	568	yield management systems (YMS)	578
keystoning	583	profit maximization	583		

Exercises

APPLICATION EXERCISE

Reliance on price as a predictor of quality seems to occur for all products. Does this mean that high-priced products are superior? Well, sometimes. Price can be a good predictor of quality for some products, but for others, price is not always the best way to determine the quality of a product or service before buying it. This exercise (and worksheet) will help you examine the price-quality relationship for a simple product: canned goods.[24]

Activities

1. Take a trip to a local supermarket where you are certain to find multiple brands of canned fruits and vegetables. Pick a single type of vegetable or fruit you like, such as cream corn or peach halves, and list five or six brands in the following worksheet:

		Price				
(1) Brand	(2) Quality/ Rank (y)	(3) Price/ Weight	(4) Price per Ounce	(5) Price Rank (x)	(6) $d\,(y-x)$	(7) d^2
Total						

2. Before going any further, rank the brands according to which you think is the highest quality (1) to the lowest quality (5 or 6, depending on how many brands you find). This ranking will be *y*.
3. Record the price and the volume of each brand. For example, if a 14-ounce can costs $.89, you would list $.89/14 oz.
4. Translate the price per volume into price per ounce. Our 14-ounce can costs $.064 per ounce.
5. Now rank the price per ounce (we'll call it *x*) from the highest (1) to the lowest (5 or 6, again depending on how many brands you have).
6. We'll now begin calculating the coefficient of correlation between the price and quality rankings. The first step is to subtract *x* from *y*. Enter the result, *d*, in column 6.
7. Now calculate d^2 and enter the value in column 7. Write the sum of all the entries in column 7 in the final row.
8. The formula for calculating a price-quality coefficient *r* is as follows:

   In the formula, r_s is the coefficient of correlation, 6 is a constant, and *n* is the number of items ranked.

$$r_s = 1 - \frac{6\sum d^2}{(n^3 - n)}$$

9. What does the result of your calculation tell you about the correlation between the price and the quality of the canned vegetable or fruit you selected? Now that you know this, will it change your buying habits?

ETHICS

ETHICS EXERCISE

Advanced Bio Medics (ABM) has invented a new stem-cell-based drug that will arrest even advanced forms of lung cancer. Development costs were actually quite low because the drug was an accidental discovery by scientists working on a different project. To stop the disease requires a regimen of one pill per week for 20 weeks. There is no substitute offered by competitors. ABM is thinking that it could maximize its profits by charging $10,000 per pill. Of course, many people will die because they can't afford the medicine at this price.

Questions

1. Should ABM maximize its profits?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketingpower.com** and review the code. Then, write a brief paragraph on what the AMA Statement of Ethics contains that relates to ABM's dilemma.

PR NEWSFOTO/©VISTO CORPORATION

Case Study: Apple iPhone

LIFE IN THE TECHNOLOGY LANE

Before Apple introduced the iPhone, it was hard for most people to imagine that they'd ever pay as much as $599 for a cell phone. But on June 29, 2007, Apple customers stood in line for hours to do just that, eager to be among the first to get their hands on the sleek new device dubbed "the God machine." *Newsweek* columnist Steven Levy described how the proud new owners were "lofting their newly acquired iPhones in the air like they'd won the Stanley Cup." Within the first three days alone, Apple sold 270,000 iPhones at premium prices ($499 for a 4GB model, $599 for 8GB), and CEO Steve Jobs was predicting that they'd cross the 10-million mark by the end of 2008.

Industry analyst Lev Grossman says that Jobs, who had already revolutionized the portable music player market with the iPod, turned his attention to mobile phones because he believed they were "broken." And Jobs likes things that are broken, Grossman says. "It means he can make something that isn't and sell it to you for a premium price." And members of the "Apple Nation" have proven that they are willing to pay.

In a company of 20,000 employees, Apple has only one committee, and its job is to establish prices. In September of 2007, Jobs announced the decision to slash the price of the iPhone, even though it had only been 68 days since its launch. Company research had shown that it was priced too high for holiday shoppers. "If we don't take that chance, we wait a whole other year," Jobs explained. "We're willing to make less money to get more iPhones out there." The same iPhone that had sold for $599 would now cost $399. At the same press conference in San Francisco, Jobs introduced the new iPod nano, the iPod classic, and the iPod touch. The only thing that made headlines, however, was the unexpected iPhone price cut and stories of the consumer outrage that followed.

Elaine Soloway, a longtime Mac user, said, "Apple really infuriated their fans, the people who urge other people to buy Apple products. We are ambassadors for them." Like Soloway, thousands of iPhone early adopters expressed their disappointment.

"This is life in the technology lane," Jobs said in an attempt to defend the company's decision to drop the price so soon. "There is always something better and less expensive on the horizon." Some call it the curse of the early adopter. But usually they get bragging rights for more than two months before the masses can afford to buy the same product they paid a premium for. In an attempt to appease his angry customers, Jobs announced that those who paid the original price would now be eligible for a $100 refund in the form of store credit.

The store credit pleased some but wasn't enough for others. One customer, who bought his iPhone only weeks before the price drop, said the $100 was merely a pay-off for being a sucker. "Steve Jobs actually put a price tag on my suckerdom—$200—and now he's trying to drain off some of that embarrassment."

The price cut didn't just disappoint Apple's core customers. Investors were concerned, as well, suspecting that the iPhone wasn't selling as well as expected. Apple shares immediately fell $1.75 to $135.01 after the announcement. Industry analysts suggest that the price change could indicate that Apple, which has long been immune to the pricing wars among other personal computer companies, may have found the cell phone business more competitive than anticipated. Whatever the reasons, Jobs acknowledged, "We need to do a better job of taking care of our early iPhone customers as we aggressively go after new ones with a lower price."

The Cult of Mac shows no sign of waning in the aftermath of the company's rare misstep, however. Customers love their iPhones, they say, and remain devoted to Apple as the arbiter of cutting-edge technology that is intuitively and beautifully designed. Sure, admits one loyal customer, "It sucks. But if they had told me then they were going to drop the price in a few months, I still would have bought it. I was obsessed."[25]

Questions

1. Apple CEO Steve Jobs alluded to the price a customer may have to pay to own an iPhone when he said that the steep and sudden price change was simply part of "life in the technology lane." What did he mean? Beyond the simple exchange of money, what else might the price of such a product include?
2. Discuss the role that product demand played in pricing the iPhone. How did this demand influence Apple's decision to price it high in the beginning and then lower it two months later?
3. Discuss how the availability of substitutes affects elasticity of demand for Apple products such as the iPhone.
4. How do you think the relationship of price to quality affects how customers perceive Apple products?

Company Clips

ACID+ALL = SERIOUS PRICING

As long as people have stomach aches, companies will sell remedies. Acid+All is banking that America will continue its love affair with bad food and has made an interesting move into the antacid market. The tiny pills come packaged in a tin priced at $3.89, which clearly sets the product apart from competitors like Rolaids, Tums, and others. The gambit of staking out a position as a prestige product is high. Watch the video to see what issues helped forge the $3.89 unit price and if the company has been successful at this price point.

Questions

1. How do the product, place, and promotion elements of Acid+All's marketing mix influence the pricing strategy the company has chosen?
2. Would you expect demand for Acid+All to be elastic? Why or why not?
3. What role do the product life cycle, competition, and perceptions of quality play in Acid+All's suggested retail price?
4. Would you buy Acid+All for the $3.89 retail price? Why or why not?

Marketing & You Results

High scores on this poll relate to a belief that you'll get more enjoyment and make better impressions if you buy high-priced brands. That is, you have a higher prestige sensitivity than someone with a lower score. If your score was low, compare it with your score for the Chapter 18 poll, which was probably high. That's because people with lower prestige sensitivities are more likely to use coupons!

Setting the Right Price

CHAPTER

20

Learning Outcomes

LO 1 Describe the procedure for setting the right price

LO 2 Identify the legal and ethical constraints on pricing decisions

LO 3 Explain how discounts, geographic pricing, and other pricing tactics can be used to fine-tune the base price

LO 4 Discuss product line pricing

LO 5 Describe the role of pricing during periods of inflation and recession

LO 1

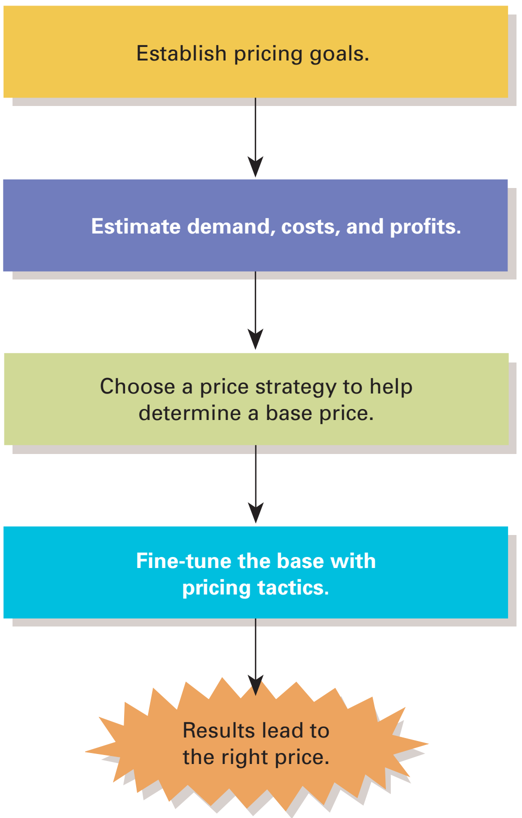
How to Set a Price on a Product or Service

Setting the right price on a product is a four-step process (see Exhibit 20.1):

1. Establish pricing goals.
2. Estimate demand, costs, and profits.
3. Choose a price strategy to help determine a base price.
4. Fine-tune the base price with pricing tactics.

The first three steps are discussed next; the fourth step is discussed later in the chapter.

Exhibit 20.1
Steps in Setting the Right Price on a Product



ESTABLISH PRICING GOALS

The first step in setting the right price is to establish pricing goals. Recall from Chapter 19 that pricing objectives fall into three categories: profit oriented, sales oriented, and status quo. These goals are derived from the firm's overall objectives. If, for example, a company's objective is to be the dominant sales leader in an industry, then it will pursue a sales-oriented market share pricing goal. A conservative organization that is attempting to lower risks by being a follower, rather than attempting to be a market leader, may establish a status quo goal. This company is simply trying to preserve its position in the marketplace. Finally, a company committed to maximizing shareholder value will establish aggressive profit-oriented pricing goals.

A good understanding of the marketplace and of the consumer can sometimes tell a manager very quickly whether a goal is realistic. For example, if firm A's objective is a 20 percent target return on investment (ROI), and its product development and implementation costs are $20 million, the market must be rather large or must support the price required to earn a 20 percent ROI. Assume that company B has a pricing objective that all new products must reach at least 15 percent market share within three years after their introduction.

Marketing & You

How price conscious are you?

Enter your answers on the lines provided.

1	2	3	4	5	6	7
Strongly disagree						Strongly agree

— I shop a lot for "specials."

— I find myself checking the prices in the grocery store even for small items.

— I usually watch the advertisements for announcements of sales.

— A person can save a lot of money by shopping around for bargains.

— I check the prices even for inexpensive items.

— I pay attention to sales and specials.

— Clothing, furniture, appliances—whatever I buy, I shop around to get the best prices.

— I usually purchase the cheapest item.

— I usually purchase items on sale only.

Total your score, and find out what it means at the end of the chapter.

A thorough study of the environment may convince the marketing manager that the competition is too strong and the market share goal can't be met.

All pricing objectives have trade-offs that managers must weigh. A profit maximization objective may require a bigger initial investment than the firm can commit or wants to commit. Reaching the desired market share often means sacrificing short-term profit because without careful management, long-term profit goals may not be met. Meeting the competition is the easiest pricing goal to implement. But can managers really afford to ignore demand and costs, the life-cycle stage, and other considerations? When creating pricing objectives, managers must consider these trade-offs in light of the target customer, the environment, and the company's overall objectives.

ESTIMATE DEMAND, COSTS, AND PROFITS

Chapter 19 explained that total revenue is a function of price and quantity demanded and that quantity demanded depends on elasticity. After establishing pricing goals, managers should estimate total revenue at a variety of prices. Next, they should determine corresponding costs for each price. They are then ready to estimate how much profit, if any, and how much market share can be earned at each possible price. These data become the heart of the developing price policy. Managers can study the options in light of revenues, costs, and profits. In turn, this information can help determine which price can best meet the firm's pricing goals.

CHOOSE A PRICE STRATEGY

price strategy
A basic, long-term pricing framework, which establishes the initial price for a product and the intended direction for price movements over the product life cycle.

The basic, long-term pricing framework for a good or service should be a logical extension of the pricing objectives. The marketing manager's chosen price strategy defines the initial price and gives direction for price movements over the product life cycle.

The price strategy sets a competitive price in a specific market segment, based on a well-defined positioning strategy. Changing a price level from premium to superpremium may require a change in the product itself, the target customers served, the promotional strategy, or the distribution channels. Thus, changing a price strategy can require dramatic alterations in the marketing mix. A carmaker cannot successfully compete in the superpremium category if the car looks and drives like an economy car.

A company's freedom in pricing a new product and devising a price strategy depends on the market conditions and the other elements of the marketing mix. If a firm launches a new item resembling several others already on the market, its pricing freedom will be restricted. To succeed, the company will probably have to charge a price close to the average market price. In contrast, a firm that introduces a totally new product with no close substitutes will have considerable pricing freedom.

Most companies do not do a good job of doing research to create a price strategy. A recent study found that only about 8 percent of the companies surveyed conducted serious pricing research to support the development of an effective pricing strategy. In fact, 88 percent of them did little or no serious pricing research. McKinsey & Co.'s Pricing Benchmark Survey estimated that only about 15 percent of companies do serious pricing research. A Coopers & Lybrand study found that 87 percent of the surveyed companies had changed prices in the previous year. Only 13 percent of the price changes, however, came after a scheduled review of pricing strategy.[1]

These numbers indicate that strategic pricing decisions tend to be made without an understanding of the likely buyer or the competitive response. Further, the research shows that managers often make tactical pricing decisions without reviewing how they may fit into the firm's overall pricing or marketing strategy. The data suggest that many companies make pricing decisions and changes

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without an existing process for managing the pricing activity. As a result, many of them do not have a serious pricing strategy and do not conduct pricing research to develop their strategy.[2]

Companies that do serious planning for creating a price strategy can select from three basic approaches: price skimming, penetration pricing, and status quo pricing. A discussion of each type follows.

Price Skimming

price skimming
A pricing policy whereby a firm charges a high introductory price, often coupled with heavy promotion. Over time, the price is often lowered as competition enters the marketplace.

Price skimming is sometimes called a "market-plus" approach to pricing because it denotes a high price relative to the prices of competing products. The term **price skimming** is derived from the phrase "skimming the cream off the top." Companies often use this strategy for new products when the product is perceived by the target market as having unique advantages. For example, Caterpillar sets premium prices on its construction equipment to support and capture its high perceived value. Genzyme Corporation introduced Ceredase as the first effective treatment for Gaucher's disease. The pill allows patients to avoid years of painful physical deterioration and lead normal lives. The cost of a year's supply for one patient can exceed $300,000.

Often companies will use skimming initially and then lower prices over time. This is called "sliding down the demand curve." Hardcover book publishers, such as HarperCollins and Random House, lower the price when the books are re-released in paperback. Calloway lowers the price of its old model golf clubs as new models hit the sales floor. Yet some manufacturers like Porsche and Cuisinart, the maker of kitchen appliances, maintain skimming prices throughout a product's life cycle. A manager of the factory that produces Chanel purses (retailing for over $2,000 each) told one of your authors that the company takes back unsold inventory and destroys it rather than selling it at a discount. Retailers such as Tiffany and Talbot's maintain skimming policies. Though both retailers occasionally have sales, their basic price strategy is price skimming.

Price skimming works best when the market is willing to buy the product even though it carries an above-average price. If, for example, some purchasing agents feel that Caterpillar equipment is far superior to competitors' products, then Caterpillar can charge premium prices successfully. Firms can also effectively use price skimming when a product is well protected legally, when it represents a technological breakthrough, or when it has in some other way blocked the entry of competitors. Managers may follow a skimming strategy when production cannot be expanded rapidly because of technological difficulties, shortages, or constraints imposed by the skill and time required to produce a product. As long as demand is greater than supply, skimming is an attainable strategy.

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Often companies will abandon a skimming strategy over time, but at Chanel that is not the case. Managers destroy unsold inventory as a way to maintain higher prices and avoid any suggestion of putting product on the market at a discount.

A successful skimming strategy enables management to recover its product development or "educational" costs quickly. (Often consumers must be "taught" the advantages of a radically new item, such as Dolby noise-canceling headphones.) Even if the market perceives an introductory price as too high, managers can easily correct the problem by lowering the price. Firms often feel it is better to test the market at a high price and then lower the price if sales are too slow. They are tacitly saying, "If there are any premium-price buyers in the market, let's reach them first and maximize our revenue per unit." Successful skimming strategies are not limited to products. Well-known athletes, entertainers, lawyers, and hairstylists are experts at price skimming. Naturally, a skimming strategy will encourage competitors to enter the market.

Above all, if price skimming is to be successful, customers must perceive a high value for the product or service. Otherwise, failure can come at a high price. Iridium phones are an example of a technology-driven, feature-loaded, high-cost, high-price innovation. The phones were billed as a "use anywhere" mobile phone system. The original developers of the system poured $5 billion into a 66-satellite system. But phones and needed accessories took up so much space that they required a special briefcase. The purchase price for a phone system was $3,000, and airtime fees were $7 per minute. At the same time, cellular phones—with more limited coverage but adequate for many customers—were selling for less than $100 and were much more "user friendly." Though the Iridium system was technologically brilliant, it was clear from its inception that customers would neither pay the high purchase price nor accept the high user fees. Approximately 50,000 customers purchased phone systems, but this was well below the volume required to sustain the business. The original owners sold the system for $25 million.[3]

Penetration Pricing

Penetration pricing is at the opposite end of the spectrum from skimming. **Penetration pricing** means charging a relatively low price for a product in order to reach the mass market. The low price is designed to capture a large share of a substantial market, resulting in lower production costs. If a marketing manager has made obtaining a large market share the firm's pricing objective, penetration pricing is a logical choice.

penetration pricing
A pricing policy whereby a firm charges a relatively low price for a product initially as a way to reach the mass market.

Penetration pricing does mean lower profit per unit, however. Therefore, to reach the break-even point, it requires a higher volume of sales than would a skimming policy. If reaching a high volume of sales takes a long time, then the recovery of product development costs will also be slow. As you might expect, penetration pricing tends to discourage competition.

Procter & Gamble examined the electric toothbrush market and noted that most electric brushes cost over $50. The company brought out the Crest SpinBrush that works on batteries and sells for just $5. It is now the nation's best-selling toothbrush, manual or electric, and has helped the Crest brand of products become P&G's twelfth billion-dollar brand.[4]

PR NEWSFOTO/© DOLLAR GENERAL CORP.

Dollar General, like most dollar stores, sells staple products at cut-rate prices. Dollar stores are now one of the fastest-growing retailers in America. The chains can put their much smaller stores right in downtown neighborhoods, closer to where people live.

A penetration strategy tends to be effective in a price-sensitive market. Price should decline more rapidly when demand is elastic because the market can be expanded through a lower price. Also, price sensitivity and greater competitive pressure should lead to a lower initial price and a relatively slow decline in the price later or to a stable low price.

Although Wal-Mart is associated with penetration pricing, other chains have done an excellent job of following this strategy as well. Dollar stores, those bare-bones, strip-mall chains that sell staples at cut-rate prices, are now one of the fastest-growing retailers in America. They've become an alternative for a growing legion of shoppers who find Wal-Mart a bit too pricey or a bit too hard to get to. Led by Dollar General, Family Dollar, and Dollar Tree, the sector adds about 1,500 stores per year. Wal-Mart usually opens its huge stores on the edge of town. Dollar chains can put their much smaller stores right in downtown neighborhoods, closer to where people live. Parking is usually a snap, and shoppers can be in and out in less time than it takes to hike across a jumbo Wal-Mart lot. And as their name implies, the dollar stores offer low prices, sometimes even beating Wal-Mart. "Wal-Mart competes on price and assortment," says David A. Perdue, Dollar General's chief executive. "We compete on price and convenience."[5]

Dollar stores cut costs to the bone to be competitive with Wal-Mart. Family Dollar, for instance, prints one advertising circular a year. The stores approach labor the same way: Dollar General and Family Dollar employ about four people per store. And all the chains rely on closeout and stock-overrun merchandise for a portion of sales.

If a firm has a low fixed cost structure and each sale provides a large contribution to those fixed costs, penetration pricing can boost sales and provide large increases in profits—but only if the market size grows or if competitors choose not to respond. Low prices can attract additional buyers to the market. The increased sales can justify production expansion or the adoption of new technologies, both of which can reduce costs. And, if firms have excess capacity, even low-priced business can provide incremental dollars toward fixed costs.

Penetration pricing can also be effective if an experience curve will cause costs per unit to drop significantly. The experience curve proposes that per-unit costs will go down as a firm's production experience increases. On average, for each doubling of production, a firm can expect per-unit costs to decline by roughly 20 percent. Cost declines can be significant in the early stages of production. Manufacturers that fail to take advantage of these effects will find themselves at a competitive cost disadvantage relative to others that are further along the curve.

The big advantage of penetration pricing is that it typically discourages or blocks competition from entering a market. The disadvantage is that penetration means gearing up for mass production to sell a large volume at a low price. What if the volume fails to materialize? The company will face huge losses from building or converting a factory to produce the failed product. Skimming, in contrast, lets a firm "stick its toe in the water" and see if limited demand exists at the high price. If not, the firm can simply lower the price. Skimming lets a company start out with a small production facility and expand it gradually as price falls and demand increases.

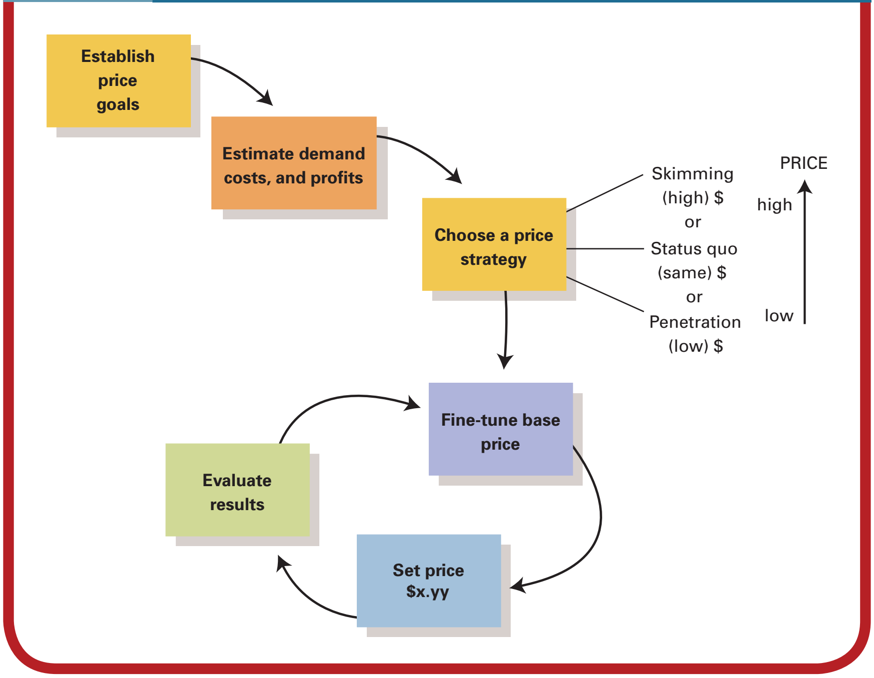
Penetration pricing can also prove disastrous for a prestige brand that adopts the strategy in an effort to gain market share and fails. When Omega—once a more prestigious brand than Rolex—was trying to improve the market share of its watches, it adopted a penetration pricing strategy that succeeded in destroying the watches' brand image by flooding the market with lower-priced products. Omega never gained sufficient share on its lower-priced/lower-image competitors to justify destroying its brand image and high-priced position with upscale buyers. Lacoste clothing experienced a similar outcome from a penetration pricing strategy.

Status Quo Pricing

The third basic price strategy a firm may choose is status quo pricing, also called meeting the competition or going rate pricing (see also Chapter 19). It means charging a price identical to or very close to the competition's price. JCPenney, for example, makes sure it is charging comparable prices by sending representatives to shop at similar retailers.

REVIEW LEARNING OUTCOME

LO 1 Describe the procedure for setting the right price



Although status quo pricing has the advantage of simplicity, its disadvantage is that the strategy may ignore demand or cost or both. If the firm is comparatively small, however, meeting the competition may be the safest route to long-term survival.

LO 2 The Legality and Ethics of Price Strategy

As we mentioned in Chapter 4, some pricing decisions are subject to government regulation. Before marketing managers establish any price strategy, they should know the laws that limit their decision making. Among the issues that fall into this category are unfair trade practices, price fixing, price discrimination, and predatory pricing.

UNFAIR TRADE PRACTICES

unfair trade practice acts
Laws that prohibit wholesalers and retailers from selling below cost.

price fixing
An agreement between two or more firms on the price they will charge for a product.

In over half the states, unfair trade practice acts put a floor under wholesale and retail prices. Selling below cost in these states is illegal. Wholesalers and retailers must usually take a certain minimum percentage markup on their combined merchandise cost and transportation cost. The most common markup figures are 6 percent at the retail level and 2 percent at the wholesale level. If a specific wholesaler or retailer can provide "conclusive proof" that operating costs are lower than the minimum required figure, lower prices may be allowed.

The intent of unfair trade practice acts is to protect small local firms from giants like Wal-Mart and Target, which operate very efficiently on razor-thin profit margins. State enforcement of unfair trade practice laws has generally been lax, however, partly because low prices benefit local consumers.

PRICE FIXING

Price fixing is an agreement between two or more firms on the price they will charge for a product. For instance, two or more executives from competing firms might meet to decide how much to charge for a product or to decide which of them will submit the lowest bid on a certain contract. Such practices are illegal under the Sherman Act and the Federal Trade Commission Act. Offenders have received fines and sometimes prison terms. Price fixing is one area where the law is quite clear, and the Justice Department's enforcement is vigorous.

Chinese manufacturers currently supply more than 85 percent of the vitamin C used in the U.S. Just like the oil cartel, they can heavily influence world prices. After an agreement among China's four largest producers, spot prices for vitamin C rose to as high as $9 a kilogram from lows of less than $3. Chinese companies deny breaking U.S. law and have hired U.S. law firms to mount a defense. The companies are expected to argue they are acting as agents of the Chinese government and therefore aren't subject to American laws against price fixing.[6]

In 2006, several major air-cargo carriers were raided by U.S. and European antitrust enforcers as part of a trans-Atlantic investigation into possible price-fixing and collusion in air cargo. Federal Bureau of Investigation agents raided British Airways facilities at New York's Kennedy Airport. Other carriers questioned were Air France-KLM, Lufthansa, American Airlines, Japan Airlines, and Scandinavian Airlines.[7] By late 2007, Air France-KLM had already spent $13 million in legal fees fighting the allegations.[8] British Airways decided not to fight the lawsuit anymore and paid $690 million to settle the charges.[9]

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Similarly, Fresh Del Monte Produce paid $3 million on fixing the price of bananas. In a little over a year, the price of bananas jumped from $5.40 a box to more than $10 a box. Settlements of $2.5 million were also reached with Chiquita Brands and Dole Food.[10]

Price-fixing prosecution is not limited to huge, global competitors. In San Diego, two groups of anesthesiologists recently settled federal charges that they conspired to set prices for Sharp Grossmont Hospital.[11]

Most price-fixing cases focus on high prices charged to customers. A reverse form of price fixing occurs when powerful buyers force their suppliers' prices down. Recently, Maine blueberry growers alleged that four big processors conspired to push down the price they would pay for fresh wild berries. A state court jury agreed and awarded millions in damages. In South Carolina, International Paper Company faces a lawsuit alleging that it conspired with its timber buyers to depress softwood prices in several states. In Alabama and Pennsylvania, federal antitrust enforcers targeted insurance companies that imposed contracts forcing down fees charged by doctors and hospitals. The insurers abandoned the practice.[12]

Resale Price Maintenance

resale price maintenance
A manufacturer, and its distributors, agree that retailers will sell products at a certain price floor.

Resale price maintenance is the practice whereby a manufacturer and its distributors agree that the retailers will sell the producer's product at a certain price (resale price maintenance), at or above a price floor. These rules prevent retailers from competing too fiercely on price and thus driving down profits. Some argue that the manufacturer may do this because it wishes to keep retailers profitable, and thus keep the manufacturer profitable. Others contend that minimum resale price maintenance, for instance, ensures that distributors who invest in promoting the manufacturer's product are able to recoup the additional costs of the promotion in the price they charge consumers. Some manufacturers also defend resale price maintenance by saying it ensures fair returns for all. The primary negative argument is that resale price maintenance results in higher consumer prices because efficient retailers, such as Wal-Mart, Costco, or Best Buy must sell at a higher price than they would normally charge.

For almost 100 years, resale price maintenance has been illegal under the Sherman Antitrust Act because it was viewed as *horizontal price fixing* (price fixing at the same level—such as two or more retailers). The Supreme Court said that it was illegal per se, meaning that resale price maintenance was illegal without regard to its impact on the market place or consumers. Then in July 2007, the Supreme Court abandoned the per se rule and said that, instead, resale price maintenance agreements should be judged by a "rule of reason" analysis. That is, a balancing of pro-competitive justifications and anti-competitive harms. Critics say that the new ruling will give manufacturers the ability to raise prices and this will hurt consumers.

Other scholars say the new ruling will have a minimal impact. "If you raise the price, you sacrifice volume," says Jeremy Anwyl, chief executive of Edmunds.com, an automobile pricing service. Only in certain cases, such as high-end goods, will an impact be felt, say experts. In the case of exotic makers, such as Bentley or

Mercedes, these companies already control prices by limiting supplies, according to Mr. Anwyl. Auto dealers could get around minimum price requirements for vehicles where demand is weak and inventories high, for instance, by paying more for a trade-in. "One way or the other dealers will adjust pricing to the market or sales will stall," he says.[13]

Makers of books, toiletries and towels also could find it difficult to flex their new pricing muscle with retailers such as Wal-Mart or Target Corp., for fear of losing their business. Just as Wal-Mart bargains hard for what it pays for merchandise, it will be able to bargain with manufacturers to keep its discounts.

PRICE DISCRIMINATION

The Robinson-Patman Act of 1936 prohibits any firm from selling to two or more different buyers, within a reasonably short time, commodities (not services) of like grade and quality at different prices where the result would be to substantially lessen competition. The act also makes it illegal for a seller to offer two buyers different supplementary services and for buyers to use their purchasing power to force sellers into granting discriminatory prices or services.

Six elements are therefore needed for a violation of the Robinson-Patman Act to occur:

- There must be price discrimination; that is, the seller must charge different prices to different customers for the same product.
- The transaction must occur in interstate commerce.
- The seller must discriminate by price among two or more purchasers; that is, the seller must make two or more actual sales within a reasonably short time.
- The products sold must be commodities or other tangible goods.
- The products sold must be of like grade and quality, not necessarily identical. If the goods are truly interchangeable and substitutable, then they are of like grade and quality.
- There must be significant competitive injury.

The Robinson-Patman Act provides three defenses for the seller charged with price discrimination (in each case the burden is on the defendant to prove the defense):

- *Cost:* A firm can charge different prices to different customers if the prices represent manufacturing or quantity discount savings.
- *Market conditions:* Price variations are justified if designed to meet fluid product or market conditions. Examples include the deterioration of perishable goods, the obsolescence of seasonal products, a distress sale under court order, and a legitimate going-out-of-business sale.
- *Competition:* A reduction in price may be necessary to stay even with the competition. Specifically, if a competitor undercuts the price quoted by a seller to a buyer, the law authorizes the seller to lower the price charged to the buyer for the product in question.

PREDATORY PRICING

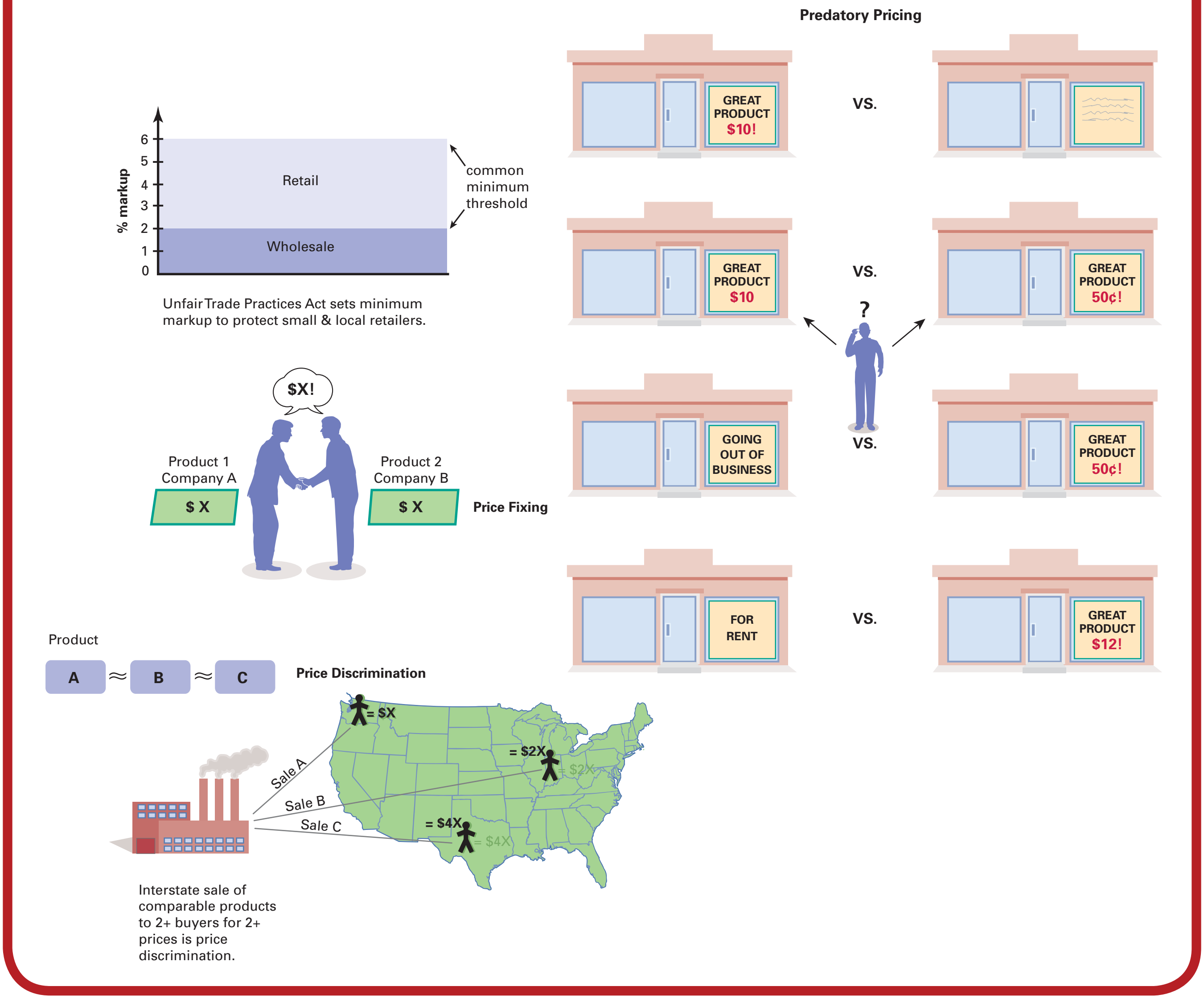
predatory pricing
The practice of charging a very low price for a product with the intent of driving competitors out of business or out of a market.

Predatory pricing is the practice of charging a very low price for a product with the intent of driving competitors out of business or out of a market. Once competitors have been driven out, the firm raises its prices. This practice is illegal under the Sherman Act and the Federal Trade Commission Act. Proving predatory pricing is difficult and expensive, however. The Justice Department must demonstrate that the predator, the destructive company, explicitly tried to ruin a competitor and that the predator's intent was to raise prices to recover its losses once competitors had been driven out of business. The U.S. Supreme Court recently noted, "Predatory pricing is rarely tried and even more rarely successful."[14] The Court also said that lowering prices typically signals legitimate competition.

Predatory bidding is similar to predatory pricing and is held to the same legal standards. In a recent case of Weyerhaeuser versus Ross-Simmons Hardwood Lumber Company, Ross-Simmons claimed that Weyerhaeuser had driven them out of business. Ross Simmons had operated a single sawmill in the Pacific Northwest since 1962. The mill purchased alder logs and processed them into finished lumber. Logs can account for up to 75 percent of a mill's cost. Weyerhaeuser entered the Pacific Northwest in 1980 and opened six mills. Ross-Simmons claimed that Weyerhaeuser deliberately overpaid for raw alder logs in order to raise the prices that Ross-Simmons had to pay for logs. By artificially "bidding up" log costs,

REVIEW LEARNING OUTCOME

LO 2 Identify the legal and ethical constraints on pricing decisions



Weyerhauser drove Ross-Simmons to declare bankruptcy. The Court held in favor of Weyerhaeuser noting that there are many reasons why the company may have bid up the price of alder logs. It could have been miscalculation, part of a risk strategy, or in response to increased consumer demand for the final product.[15]

LO 3

Tactics for Fine-Tuning the Base Price

base price
The general price level at which the company expects to sell the good or service.

quantity discount
A price reduction offered to buyers buying in multiple units or above a specified dollar amount.

cumulative quantity discount
A deduction from list price that applies to the buyer's total purchases made during a specific period.

noncumulative quantity discount
A deduction from list price that applies to a single order rather than to the total volume of orders placed during a certain period.

cash discount
A price reduction offered to a consumer, an industrial user, or a marketing intermediary in return for prompt payment of a bill.

functional discount (trade discount)
A discount to wholesalers and retailers for performing channel functions.

seasonal discount
A price reduction for buying merchandise out of season.

After managers understand both the legal and the marketing consequences of price strategies, they should set a base price, the general price level at which the company expects to sell the good or service. The general price level is correlated with the pricing policy: above the market (price skimming), at the market (status quo pricing), or below the market (penetration pricing). The final step, then, is to fine-tune the base price.

Fine-tuning techniques are short-run approaches that do not change the general price level. They do, however, result in changes within a general price level. These pricing tactics allow the firm to adjust for competition in certain markets, meet ever-changing government regulations, take advantage of unique demand situations, and meet promotional and positioning goals. Fine-tuning pricing tactics include various sorts of discounts, geographic pricing, and other pricing tactics.

DISCOUNTS, ALLOWANCES, REBATES, AND VALUE-BASED PRICING

A base price can be lowered using discounts and the related tactics of allowances, rebates, low or zero percent financing, and value-based pricing. Managers use the various forms of discounts to encourage customers to do what they would not ordinarily do, such as paying cash rather than using credit, taking delivery out of season, or performing certain functions within a distribution channel.[16] The following are of the most common tactics:

- *Quantity discounts:* When buyers get a lower price for buying in multiple units or above a specified dollar amount, they are receiving a quantity discount. A cumulative quantity discount is a deduction from list price that applies to the buyer's total purchases made during a specific period; it is intended to encourage customer loyalty. In contrast, a noncumulative quantity discount is a deduction from list price that applies to a single order rather than to the total volume of orders placed during a certain period. It is intended to encourage orders in large quantities.
- *Cash discounts:* A cash discount is a price reduction offered to a consumer, an industrial user, or a marketing intermediary in return for prompt payment of a bill. Prompt payment saves the seller carrying charges and billing expenses and allows the seller to avoid bad debt.
- *Functional discounts:* When distribution channel intermediaries, such as wholesalers or retailers, perform a service or function for the manufacturer, they must be compensated. This compensation, typically a percentage discount from the base price, is called a functional discount (or trade discount). Functional discounts vary greatly from channel to channel, depending on the tasks performed by the intermediary.
- *Seasonal discounts:* A seasonal discount is a price reduction for buying merchandise out of season. It shifts the storage function to the purchaser. Seasonal discounts also enable manufacturers to maintain a steady production schedule year-round.

promotional allowance (trade allowance)
A payment to a dealer for promoting the manufacturer's products.

rebate
A cash refund given for the purchase of a product during a specific period.

markdown money
A payment by a manufacturer to a retailer to help cover the costs of markdowns that the retailer had to take.

- *Promotional allowances:* A promotional allowance (also known as a trade allowance) is a payment to a dealer for promoting the manufacturer's products. It is both a pricing tool and a promotional device. As a pricing tool, a promotional allowance is like a functional discount. If, for example, a retailer runs an ad for a manufacturer's product, the manufacturer may pay half the cost. If a retailer sets up a special display, the manufacturer may include a certain quantity of free goods in the retailer's next order.[17]

- *Rebates:* A rebate is a cash refund given for the purchase of a product during a specific period. The advantage of a rebate over a simple price reduction for stimulating demand is that a rebate is a temporary inducement that can be taken away without altering the basic price structure. A manufacturer that uses a simple price reduction for a short time may meet resistance when trying to restore the price to its original, higher level. Fully 40 percent of all rebates never get redeemed because consumers fail to apply for them or their applications are rejected.[18] Also, complex rules, filing periods of as little as a week, repeated requests for copies of receipts, and long delays in sending out checks discourage consumers from even attempting to retrieve their money. That translates into more than $2 billion of extra revenue for retailers and their suppliers each year. What rebates do is get consumers to focus on the discounted price of a product, then buy it at full price. "The game is obviously that anything less than 100 percent redemption is free money," says Paula Rosenblum, director of retail research at consulting firm Aberdeen Group Inc.[19] The quest for consumers who never file for a rebate has resulted in new terminology. Purchases by consumers who never file for their rebates are called "breakage." Wireless companies that pay 100 percent rebates on some cell phones, for example, rely in part on "breakage" to make money. Rebate checks that are never cashed are called "slippage."

- *Zero percent financing:* During the early and mid-2000s, new-car sales needed a boost. To get people back into automobile showrooms, manufacturers offered zero percent financing, which enabled purchasers to borrow money to pay for new cars without incurring an interest charge. The tactic created a huge increase in sales but not without cost to the manufacturers. A five-year interest-free car loan represented a cost of over $3,000 on a typical vehicle sold during the zero percent promotion. Automakers were still offering such incentives in 2007.

- *Markdown money:* For decades, department stores have expected clothing companies and other merchandise suppliers to share in their sales risk. Whenever a suit or a sweater doesn't sell at full price, it is marked down. Department stores have required vendors to absorb some of the cost by paying the retailers markdown money at the end of each season. It's a perpetual negotiation in which each side moans that the other isn't shouldering enough of the risk. But recently, as department stores struggle for survival against discounters and specialty chains, vendors say certain retailers have been pushing too hard, relying too much on markdowns to move merchandise and demanding higher rebates than what were originally agreed upon. Critics say markdown allowances, while legal, create an uneven playing field for vendors. Some big, powerful suppliers hold more sway with retailers and might pay lower allowances, creating an unfair advantage over smaller ones, according to some smaller vendors. Markdown money may be onerous for suppliers, but most have no choice but to "comply because they need the business," said Madison Riley, a principal at Kurt Salmon Associates, a consumer products consulting company. "If a vendor can't help a department store improve its profit margins, department stores have plenty of alternatives."[20]

Value-Based Pricing

value-based pricing
Setting the price at a level that seems to the customer to be a good price compared to the prices of other options.

Value-based pricing, also called *value pricing*, is a pricing strategy that has grown out of the quality movement. Instead of figuring prices based on costs or competitors' prices, it starts with the customer, considers the competition, and then determines the appropriate price. The basic assumption is that the firm is customer driven, seeking to understand the attributes customers want in the goods and services they buy and the value of that bundle of attributes to customers. Because very few firms operate in a pure monopoly, however, a marketer using value-based pricing must also determine the value of competitive offerings to customers. Customers determine the value of a product (not just its price) relative to the value of alternatives. In value-based pricing, therefore, the price of the product is set at a level that seems to the customer to be a good price compared with the prices of other options.

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When two Wal-Mart Supercenters and a rival regional grocery opened near a Kroger supermarket in Houston, the Kroger's sales dropped 10 percent. The store manager moved quickly to slash some prices and cut labor costs, for example, by buying ready-made cakes instead of baking them in-house and ordering precut salad-bar items from suppliers. Kroger employees used to stack displays by hand; now fruit and vegetables arrive stacked for display.

Such moves have helped Kroger cut worker-hours by 30 to 40 percent over the last four years and lower the prices of staples such as cereal, bread, milk, eggs, and disposable diapers. If Wal-Mart's Supercenters continue to expand at their current pace, however, within this decade, more than three-quarters of the nation's Kroger's and Albertson's stores and more than half the Safeway outlets could be within ten miles of a Wal-Mart Supercenter.

The fight for the minds of customers is already having an impact. Shoppers in competitive markets are seeing prices fall as Wal-Mart pushes rivals to match its value prices. Recently, a number of regional grocery chains have switched to value pricing. In the past, they offered weekly specials to attract shoppers and then made up the lost profit by keeping nonsale prices substantially higher. Now, stores like Costco and Wal-Mart have conditioned consumers to expect inexpensive goods every day.

Ethan Allen Interiors, the furniture retailer, recently dropped its six or seven sales events each year and moved to value pricing. All retail prices are roughly 7 percent lower than the previous year. Value pricing has also eliminated some production bottlenecks and inefficiencies caused by sales-driven order surges. Despite a move to value pricing, Ethan Allen has had trouble gaining market share. Critics say price cuts haven't gone far enough. Large Chinese manufacturers are producing Ethan Allen-quality products at much lower price points.[21]

Pricing Products Too Low

Sometimes managers price their products too low, thereby reducing company profits.[22] This seems to happen for two reasons. First, managers attempt to buy market share through aggressive pricing. Usually, however, these price cuts are quickly met by competitors. Thus, any gain in market share is short-lived, and overall industry profits end up falling. Second, managers have a natural tendency to want to make decisions that can be justified objectively. The problem is that companies often lack hard data on the complex determinants of profitability, such as the relationship between price changes and sales volumes, the link between demand levels and costs, and the likely responses of competitors to price changes. In contrast, companies usually have rich, unambiguous information on costs, sales, market share, and competitors' prices. As a result, managers tend to make pricing decisions based on current costs, projected short-term share gains, or current competitor prices rather than on long-term profitability.

The problem of "underpricing" can be solved by linking information about price, cost, and demand within the same decision support system. The demand data can be developed via marketing research. This will enable managers to get the hard data they need to calculate the effects of pricing decisions on profitability.

GEOGRAPHIC PRICING

Because many sellers ship their wares to a nationwide or even a worldwide market, the cost of freight can greatly affect the total cost of a product. Sellers may use several different geographic pricing tactics to moderate the impact of freight costs on distant customers. The following methods of geographic pricing are the most common:

- *FOB origin pricing:* FOB origin pricing, also called FOB factory or *FOB shipping point,* is a price tactic that requires the buyer to absorb the freight costs from the shipping point ("free on board"). The farther buyers are from sellers, the more they pay, because transportation costs generally increase with the distance merchandise is shipped.

- *Uniform delivered pricing:* If the marketing manager wants total costs, including freight, to be equal for all purchasers of identical products, the firm will adopt uniform delivered pricing, or "postage stamp" pricing. With uniform delivered pricing, the seller pays the actual freight charges and bills every purchaser an identical, flat freight charge. L.L. Bean uses uniform delivered pricing: if you purchase something from its catalog, you will be charged a flat freight rate.
- *Zone pricing:* A marketing manager who wants to equalize total costs among buyers within large geographic areas—but not necessarily all of the seller's market area—may modify the base price with a zone-pricing tactic. Zone pricing is a modification of uniform delivered pricing. Rather than using a uniform freight rate for the entire United States (or its total market), the firm divides it into segments or zones and charges a flat freight rate to all customers in a given zone. The U.S. Postal Service's parcel post rate structure is probably the best-known zone-pricing system in the country.
- *Freight absorption pricing:* In freight absorption pricing, the seller pays all or part of the actual freight charges and does not pass them on to the buyer. The manager may use this tactic in intensely competitive areas or as a way to break into new market areas.
- *Basing-point pricing:* With basing-point pricing, the seller designates a location as a basing point and charges all buyers the freight cost from that point, regardless of the city from which the goods are shipped. Thanks to several adverse court rulings, basing-point pricing has waned in popularity. Freight fees charged when none were actually incurred, called *phantom freight,* have been declared illegal.

OTHER PRICING TACTICS

Unlike geographic pricing, other pricing tactics are unique and defy neat categorization. Thus, we simply call this group "other." Managers use these tactics for various reasons—for example, to stimulate demand for specific products, to increase store patronage, and to offer a wider variety of merchandise at a specific price point. "Other" pricing tactics include a single-price tactic, flexible pricing, professional services pricing, price lining, leader pricing, bait pricing, odd–even pricing, price bundling, and two-part pricing. A brief overview of each of these tactics follows, along with a manager's reasons for using that tactic or a combination of tactics to change the base price.

Single-Price Tactic

A merchant using a single-price tactic offers all goods and services at the same price (or perhaps two or three prices). Retailers using this tactic include One Price Clothing Stores, Dre$$ to the Nine$, Your $10 Store, and Fashions $9.99. One Price Clothing Stores, for example, tend to be small, about 3,000 square feet. Their goal is to offer merchandise that would sell for at least $15 to $18 in other stores. The

FOB origin pricing
A price tactic that requires the buyer to absorb the freight costs from the shipping point ("free on board").

uniform delivered pricing
A price tactic in which the seller pays the actual freight charges and bills every purchaser an identical, flat freight charge.

zone pricing
A modification of uniform delivered pricing that divides the United States (or the total market) into segments or zones and charges a flat freight rate to all customers in a given zone.

freight absorption pricing
A price tactic in which the seller pays all or part of the actual freight charges and does not pass them on to the buyer.

basing-point pricing
A price tactic that charges freight from a given (basing) point, regardless of the city from which the goods are shipped.

single-price tactic
A price tactic that offers all goods and services at the same price (or perhaps two or three prices).

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KeepMedia is a Web site that offers consumers unlimited access to a database of magazine articles for a flat monthly rate of $4.95. In addition to using a single-price tactic, KeepMedia's pricing strategy represents penetration pricing in a market where online articles regularly cost around $3 per article. Pictured here is KeepMedia Chairman, Louis Borders.

stores carry pants, shirts, blouses, sweaters, and shorts for juniors, misses, and large-sized women. The stores do not feature any seconds or irregular items, and everything is sold for under $10.

Single-price selling removes price comparisons from the buyer's decision-making process. The consumer just looks for suitability and the highest perceived quality. The retailer enjoys the benefits of a simplified pricing system and minimal clerical errors. However, continually rising costs are a headache for retailers following this strategy. In times of inflation, they must frequently raise the selling price.

Flexible Pricing

flexible pricing (variable pricing)
A price tactic in which different customers pay different prices for essentially the same merchandise bought in equal quantities.

Flexible pricing (or variable pricing) means that different customers pay different prices for essentially the same merchandise bought in equal quantities. This tactic is often found in the sale of shopping goods, specialty merchandise, and most industrial goods except supply items. Car dealers, many appliance retailers, and manufacturers of industrial installations, accessories, and component parts commonly follow the practice. It allows the seller to adjust for competition by meeting another seller's price. Thus, a marketing manager with a status quo pricing objective might readily adopt the tactic. Flexible pricing also enables the seller to close a sale with price-conscious consumers. If buyers show promise of becoming large-volume shoppers, flexible pricing can be used to lure their business.

The obvious disadvantages of flexible pricing are the lack of consistent profit margins, the potential ill will of high-paying purchasers, the tendency for salespeople to automatically lower the price to make a sale, and the possibility of a price war among sellers. The disadvantages of flexible pricing have led the automobile industry to experiment with one price for all buyers.

Professional Services Pricing

Professional services pricing is used by people with lengthy experience, training, and often certification by a licensing board—for example, lawyers, physicians, and family counselors. Professionals sometimes charge customers at an hourly rate, but sometimes fees are based on the solution of a problem or performance of an act (such as an eye examination) rather than on the actual time involved. A surgeon may perform a heart operation and charge a flat fee of $5,000. The operation itself may require only four hours, resulting in a hefty $1,250 hourly rate. The physician justifies the fee because of the lengthy education and internship required to learn the complex procedures of a heart operation. Lawyers also sometimes use flat-rate pricing, such as $500 for completing a divorce and $50 for handling a traffic ticket.

Those who use professional pricing have an ethical responsibility not to overcharge a customer. Because demand is sometimes highly inelastic, such as when a person requires heart surgery or a daily insulin shot to survive, there may be a temptation to charge "all the traffic will bear."[23] An alternative way to earn more money is through a form of self-referral, as explained in the "Ethics in Marketing" box.

Price Lining

price lining
The practice of offering a product line with several items at specific price points.

When a seller establishes a series of prices for a type of merchandise, it creates a price line. Price lining is the practice of offering a product line with several items at specific price points. For example, Hon, an office furniture manufacturer, may offer its four-drawer file cabinets at $125, $250, and $400. The Limited may offer women's dresses at $40, $70, and $100, with no merchandise marked at prices between those figures. Instead of a normal demand curve running from $40 to $100, The Limited has three demand points (prices). Theoretically, the "curve" exists only because people would buy goods at the in-between prices if it were possible to do so. For example, a number of dresses could be sold at $60, but no sales will occur at that price because $60 is not part of the price line.

Price lining reduces confusion for both the salesperson and the consumer. The buyer may be offered a wider variety of merchandise at each established price. Price lines may also enable a seller to reach several market segments. For buyers, the question of price may be quite simple: all they have to do is find a suitable product at the predetermined price. Moreover, price lining is a valuable tactic for the marketing manager, because the firm may be able to carry a smaller total inventory than it could without price lines. The results may include fewer markdowns, simplified purchasing, and lower inventory carrying charges.

Price lines also present drawbacks, especially if costs are continually rising. Sellers can offset rising costs in three ways. First, they can begin stocking lower-quality merchandise at each price point. Second, sellers can change the prices, although frequent price line changes confuse buyers. Third, sellers can accept lower profit margins and hold quality and prices constant. This third alternative has short-run benefits, but its long-run handicaps may drive sellers out of business.

ETHICS in Marketing

Self-Referral Can Lead to Healthy Profits for Doctors

Medical imaging such as MRI and CT scanning is one of health care's fastest-growing sectors. An owner of imaging centers told doctors how they could get in on the boom. At a meeting of cardiologists, neurologists and cancer specialists in Torrance, Calif., Imaging Solutions Inc. proposed that the doctors sign a contract to send patients to one of its centers. According to documents handed out there and physicians who attended, the deal worked this way: The center would charge doctors a flat rate per scan. Then the doctors could bill insurers at the going reimbursement rate in their area. For an MRI, the company would charge doctors $375. It pegged the average reimbursement in the region at $706.31.

After deducting the cost of having the scan interpreted, the paperwork said, the doctors would net $234.77 from each MRI. It showed that a group practice could clear $122,078 a year if it referred two patients a day for scans, or $610,390 annually if it referred 10 a day. For a less-common kind of screening known as PET scans, profits would be higher: $525,200 a year to the doctors if they made two daily referrals, or $2.6 million annually for 10 a day.

Arrangements like this are increasingly common, say some doctors, industry officials, and health-care lawyers. But few doctors acknowledge taking part in them, and the scanning centers that offer them typically are reluctant to identify referring doctors. Some lawyers say the referral deals risk running afoul of federal and state laws. Others say the arrangements risk raising usage of expensive procedures at a time when U.S. medical costs already are surging.

It's a federal crime for health-care providers to compensate doctors for referrals, or for doctors to receive such compensation, when Medicare or Medicaid patients are involved. Additionally, 36 states, including California, have enacted bans called anti-kickback laws, which extend to all other types of patients, too. Some lawyers say the doctors' almost assured profits under some imaging-center contracts might be considered illegal inducement for referral.

The arrangements also raise an issue of "self referral," which occurs when doctors refer patients to businesses in which they or relatives have a financial stake. Because this practice, like payment for referral, can encourage overuse of costly medical services, it is barred by a federal statute, in this case a civil one. But the law against self-referral has exceptions, one of which says the services are all right so long as doctors do them in their own offices. Some imaging companies structure referral deals as leases, under which doctors, each time they send over a patient, are renting the scan center's facilities and employees. Imaging firms appear to be establishing a framework to argue that doctors' offices temporarily include the imaging center, say some health-care lawyers. Donald Ryan is head of CareCore National Inc. in Wappingers Falls, N.Y., which analyzes imaging claims for insurers to help them control costs. He says, "Utilization goes through the roof" when doctors have a financial stake in providing imaging tests.[24]

Do you think that self-referral is unethical? How about a clinic that has its own lab for blood work, urinalysis, and so forth? Is this unethical? Do you think that when imaging companies structure their contracts as leases that this makes the referral process ethical?

Leader Pricing

Leader pricing (or loss-leader pricing) is an attempt by the marketing manager to attract customers by selling a product near or even below cost in the hope that shoppers will buy other items once they are in the store. This type of pricing appears weekly in the newspaper advertising of supermarkets, specialty stores, and department stores. Leader pricing is normally used on well-known items that consumers can easily recognize as bargains at the special price. The goal is not necessarily to sell large quantities of leader items, but to try to appeal to customers who might shop elsewhere.[25]

Leader pricing is not limited to products. Health clubs offer a one-month free trial as a loss leader. Lawyers give a free initial consultation. And restaurants distribute two-for-one coupons and "welcome to the neighborhood" free meal coupons.

leader pricing (loss-leader pricing)
A price tactic in which a product is sold near or even below cost in the hope that shoppers will buy other items once they are in the store.

bait pricing
A price tactic that tries to get consumers into a store through false or misleading price advertising and then uses high-pressure selling to persuade consumers to buy more expensive merchandise.

odd–even pricing (psychological pricing)
A price tactic that uses odd-numbered prices to connote bargains and even-numbered prices to imply quality.

price bundling
Marketing two or more products in a single package for a special price.

Bait Pricing

In contrast to leader pricing, which is a genuine attempt to give the consumer a reduced price, bait pricing is deceptive. Bait pricing tries to get the consumer into a store through false or misleading price advertising and then uses high-pressure selling to persuade the consumer to buy more expensive merchandise. You may have seen this ad or a similar one:

> REPOSSESSED . . . Singer slant-needle sewing machine . . . take over 8 payments of $5.10 per month . . . ABC Sewing Center.

This is bait. When a customer goes in to see the machine, a salesperson says that it has just been sold or else shows the prospective buyer a piece of junk no one would buy. Then the salesperson says, "But I've got a really good deal on this fine new model." This is the switch that may cause a susceptible consumer to walk out with a $400 machine. The Federal Trade Commission considers bait pricing a deceptive act and has banned its use in interstate commerce. Most states also ban bait pricing, but sometimes enforcement is lax.

Odd–Even Pricing

Odd–even pricing (or psychological pricing) means pricing at odd-numbered prices to connote a bargain and pricing at even-numbered prices to imply quality. For years, many retailers have priced their products in odd numbers—for example, $99.95 or $49.95—to make consumers feel they are paying a lower price for the product.

Contrary to popular belief that the ".99" part of a price such as $19.99 makes the difference in purchasing behavior, new research finds that it's the left digits—the numbers that come before the .99—that determine whether consumers perceive a penny reduction as a bargain. Research participants were shown product prices that ended either in nine (e.g., $19.99 and $23.59) or in zero (e.g., $20.00 and $23.60). In half the cases, when the price ending changed from zero to nine, the left digit changed and the price became lower (e.g., $20.00 changed to $19.99). For the other half, the left digit stayed the same (e.g., $23.60 changed to $23.59). When the left digit changed, participants thought the price with the nine ending (e.g., $19.99) was much cheaper than the price with the zero ending (e.g., $20.00). When the left digit did not change, however, participants perceived the nine- and the zero-ending prices (e.g., $23.60 versus $23.59) as essentially the same. These results demonstrate that the "left-digit effect," changing the left digits to a lower number (20 to 19) rather than the right digits (.60 to .59), is what affected the participants' perception of the price.[26]

Even-numbered pricing is sometimes used to denote quality. Examples include a fine perfume at $100 a bottle, a good watch at $500, or a mink coat at $3,000. The demand curve for such items would also be sawtoothed, except that the outside edges would represent even-numbered prices and, therefore, elastic demand.

Price Bundling

Price bundling is marketing two or more products in a single package for a special price. Examples include the sale of maintenance contracts with computer hardware

Price bundling can encourage consumers to buy more than they may have originally planned to purchase. This Xbox game system has bundled extra memory, wireless controllers, headset, and games for about $100 more than the basic unit.

© VICKI BEAVER

and other office equipment, packages of stereo equipment, packages of options on cars, weekend hotel packages that include a room and several meals, and airline vacation packages. Microsoft offers "suites" of software that bundle spreadsheets, word processing, graphics, electronic mail, Internet access, and groupware for networks of microcomputers. Price bundling can stimulate demand for the bundled items if the target market perceives the price as a good value.

Services like hotels and airlines sell a perishable commodity (hotel rooms and airline seats) with relatively constant fixed costs. Bundling can be an important income stream for these businesses because the variable cost tends to be low—for instance, the cost of cleaning a hotel room or putting one more passenger on an airplane. Therefore, most of the revenue can help cover fixed costs and generate profits.

The automobile industry has a different motive for bundling. People buy cars only every three to five years. Thus, selling options is a somewhat rare opportunity for the car dealer. Price bundling can help the dealer sell a maximum number of options.

Bundling has also been used in the telecommunications industry. Companies offer local service, long distance, DSL Internet service, wireless, and even cable TV in various menus of bundling. Such bundling is not necessarily consumer focused. Telecom companies use bundling as a way to protect their market share and fight off competition by locking customers into a group of services. Comparison shopping may be difficult for consumers since they may not be able to determine how much they are really paying for each component of the bundle.

unbundling
Reducing the bundle of services that comes with the basic product.

A related price tactic is **unbundling,** or reducing the bundle of services that comes with the basic product. Rather than raise the price of hotel rooms, some hotel chains have started charging registered guests for parking. To help hold the line on costs, some stores require customers to pay for gift wrapping.

Clearly, price bundling—for example, a theater series pass or a vacation package that combines airfare, lodging, and meals—can influence consumers' purchase behavior. But what about the decision to consume a particular bundled product or service, such as eating the daily lunch buffet or attending a particular theater performance? Some of the latest research has focused on how people consume certain bundled products or services. According to this research, the key to consumption behavior is how closely consumers can link the costs and benefits of the exchange.[27] In complex transactions like a holiday package, it may be unclear which costs are paying for which benefits. In such cases, consumers tend to mentally downplay their up-front costs for the bundled product, so they may be more likely to forgo a benefit that's part of the bundle, like a free dinner or a play.

Similarly, when people buy season tickets to a concert series, sporting event, or other activity, the sunk costs (price of the bundle) and the pending benefit (going to see an event) become decoupled. This reduces the likelihood of consumption of the event over time. For example, researchers found that theatergoers who purchased tickets to four plays were only 84 percent likely to use their first-play tickets and only 78 percent likely to use any given ticket across the four plays.[28] In contrast, theatergoers who purchased tickets to a single play were almost certain to use those tickets. This is consistent with the idea that in a one-to-one transaction (i.e., one payment, one benefit), the costs and benefits of that transaction are tightly coupled, resulting in strong sunk cost pressure to consume the pending benefit. In other words, "I bought this ticket, now I've got to use it."

In practice, these findings mean that a theater manager might expect a no-show rate of 20 percent when the percentage of season ticket holders is high, but a no-show rate of only 5 percent when the percentage of season ticket holders is low. With a high number of season ticket holders, a manager could oversell performances and maximize the revenue for the theater. Airlines routinely overbook in anticipation of a predictable percentage of no-shows.

The physical format of the transaction also figures in. A ski lift pass in the form of a booklet of tickets strengthens the cost-benefit link for consumers, whereas a single pass for multiple ski lifts weakens that link. Thus, the skier with a booklet of tickets is likely to use the ski lift more often than the skier who has just one pass for multiple lifts, even though both paid the same amount at the outset.

Though price bundling of services can result in a lower rate of total consumption of that service, the same is not necessarily true for products. Consider the purchase of an expensive bottle of wine, which can be inventoried until needed. When the wine is purchased as a single unit, its cost and eventual benefit are tightly coupled. As a result, the cost of the wine will be quite important, and a person will likely reserve that wine for a special occasion. When purchased as part of a bundle (e.g., as part of a case of wine), however, the cost and benefit of that individual bottle of wine will likely become decoupled, reducing the impact of the cost on eventual consumption. As a result, a person will likely find the wine appropriate for many more (not-so-special) occasions. Thus, in contrast to the price bundling of services, the price bundling of physical goods could lead to an increase in product consumption.

two-part pricing
A price tactic that charges two separate amounts to consume a single good or service.

consumer penalty
An extra fee paid by the consumer for violating the terms of the purchase agreement.

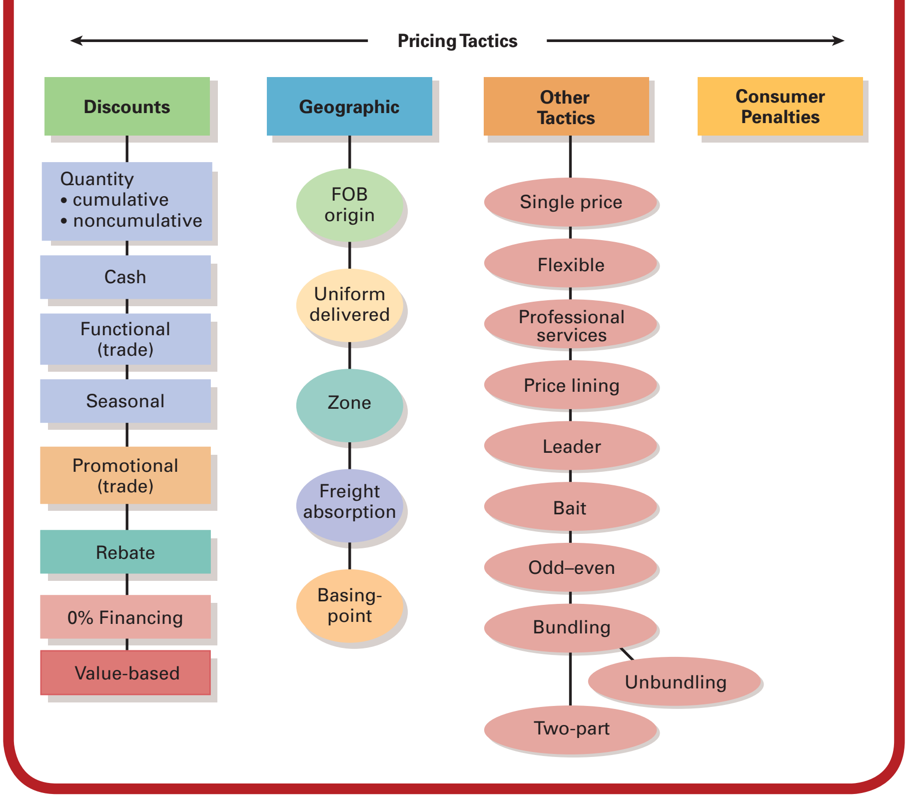
Two-Part Pricing

Two-part pricing means establishing two separate charges to consume a single good or service. Tennis clubs and health clubs charge a membership fee and a flat fee each time a person uses certain equipment or facilities. In other cases they charge a base rate for a certain level of usage, such as ten racquetball games per month, and a surcharge for anything over that amount.

Consumers sometimes prefer two-part pricing because they are uncertain about the number and the types of activities they might use at places like an amusement park. Also, the people who use a service most often pay a higher total price. Two-part pricing can increase a seller's revenue by attracting consumers who would not pay a high fee even for unlimited use. For example, a health club might be able to sell only 100 memberships at $700 annually with unlimited use of facilities, for total revenue of $70,000. However, perhaps it could sell 900 memberships at $200 with a guarantee of using the racquetball courts ten times a month. Every use over ten would require the member to pay a $5 fee. Thus, membership revenue would provide a base of $180,000, with some additional usage fees throughout the year.

REVIEW LEARNING OUTCOME

LO3 Explain how discounts, geographic pricing, and other pricing tactics can be used to fine-tune the base price



CONSUMER PENALTIES

More and more businesses are adopting **consumer penalties**—extra fees paid by consumers for violating the terms of a purchase agreement (see Exhibit 20.2).

Exhibit 20.2

Common Consumer Penalties

1. Airlines

- Some airlines charge a penalty of $100 for changing reservations on discount tickets; many airlines charge for overweight baggage or checking a second bag.

2. Automobiles

- Penalties are imposed for early terminations of car leases. In some cases, deposits on canceled leases can be subject to penalties.
- Car owners in England pay penalties, administration fees, and commissions if they cancel an insurance policy early.

3. Banks

- Penalties are often associated with early withdrawal of certificates of deposit.
- Some banks charge penalties for too many withdrawals in a month.
- Some have monthly penalties of $5 to $10 if a client's balance falls below a minimum level.
- Banks can charge late fees, in addition to interest, for tardy payments.

4. Car Rentals

- Rental companies often have $25 to $100 penalties for no-shows for specialty vehicles. Budget, National, and Dollar/Thrifty are experimenting with no-show fees on all rentals.

5. Child Day Care

- Many day-care centers charge a penalty of up to $5 a minute when parents are late in picking up their children.

6. Cellular Phones

- Companies have cancellation penalties, often in the small print on the back of a contract, that can run as high as $525.

7. Credit and Debit Cards

- Some vendors now charge late fees (beyond normal interest). Lenders collect about $2 billion in late charges each year.
- GE Rewards MasterCard charges $25 a year for those who pay their bill each month, in full, on time. Advanta credit card company may charge $25 for six-month inactivity on an account and $25 to close an account.

8. Cruises

- If a cruise is sailing, even though there are hurricane warnings, some cruise lines will assess penalties if a passenger cancels.
- Even trip cancellation insurance will not ensure a refund if the traveler has embarked on the trip.
- Britain is trying to crack down on excessive cancellation penalties on package holidays.
- The *Carnival Paradise* will disembark passengers found smoking.

9. Hotels

- Some hotels require 72 hours' cancellation notice, or the client must pay a penalty of one day's room cost.
- Most hotels have high charges for using in-room long-distance service.
- Hilton, Hyatt, and Westin have early departure fees ranging from $25 to $50.

10. Restaurants

- Some now charge up to $50 per person for no-show parties.

11. Retail Stores

- Circuit City and Best Buy are leading others in charging a 15 percent restocking fee on some returned items. A restocking fee is for putting a returned item back in inventory.

12. Trains

- Amtrak has a $20 penalty for a returned ticket and charges the same fee for changing a ticket.

13. Universities

- Some universities will give only a partial tuition refund if a student becomes ill after a course begins.

SOURCE: Eugene Fram and Michael McCarthy, "The True Price of Penalties," *Marketing Management*, Fall 1999, 51.

Businesses impose consumer penalties for two reasons: They will allegedly (1) suffer an irrevocable revenue loss and/or (2) incur significant additional transaction costs should customers be unable or unwilling to complete their purchase obligations. For the company, these customer payments are part of doing business in a highly competitive marketplace. With profit margins in many companies increasingly coming under pressure, organizations are looking to stem losses resulting from customers not meeting their obligations. However, the perceived unfairness of a penalty may affect some consumers' willingness to patronize a business in the future.

LO4

Product Line Pricing

product line pricing
Setting prices for an entire line of products.

joint costs
Costs that are shared in the manufacturing and marketing of several products in a product line.

Product line pricing is setting prices for an entire line of products. Compared to setting the right price on a single product, product line pricing encompasses broader concerns. In product line pricing, the marketing manager tries to achieve maximum profits or other goals for the entire line rather than for a single component of the line.

RELATIONSHIPS AMONG PRODUCTS

The manager must first determine the type of relationship that exists among the various products in the line:

- If items are *complementary,* an increase in the sale of one good causes an increase in demand for the complementary product, and vice versa. For example, the sale of ski poles depends on the demand for skis, making these two items complementary.
- Two products in a line can also be *substitutes* for each other. If buyers buy one item in the line, they are less likely to buy a second item in the line. For example, if someone goes to an automotive supply store and buys paste Turtle Wax for a car, it is very unlikely that he or she will buy liquid Turtle Wax in the near future.
- A *neutral* relationship can also exist between two products. In other words, demand for one of the products is unrelated to demand for the other. For instance, Ralston Purina sells chicken feed and Wheat Chex, but the sale of one of these products has no known impact on demand for the other.

JOINT COSTS

Joint costs are costs that are shared in the manufacturing and marketing of several products in a product line. These costs pose a unique problem in product pricing. In oil refining, for example, fuel oil, gasoline, kerosene, naphtha, paraffin, and lubricating oils are all derived from a common production process. Another example is the production of compact discs that combine photos and music.

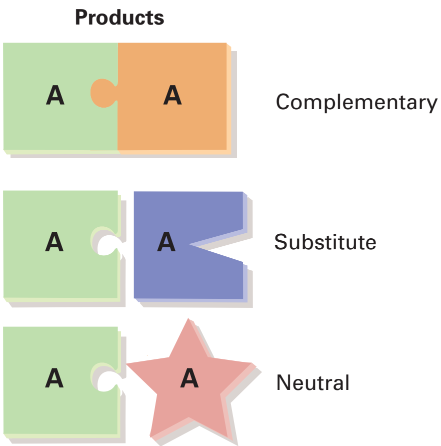
Any assignment of joint costs must be somewhat subjective because costs are actually shared. Suppose a company produces two products, X and Y, in a common production process, with joint costs allocated on a weight basis. Product X weighs 1,000 pounds, and product Y weighs 500 pounds. Thus, costs are allocated on the basis of $2 for X for every $1 for Y. Gross margins (sales less the cost of goods sold) might then be as follows:

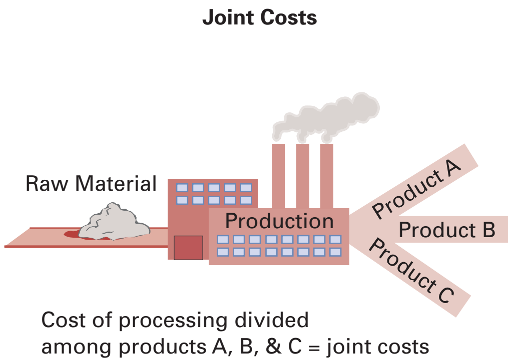
	Product X	Product Y	Total
Sales	$20,000	$6,000	$26,000
Less: cost of goods sold	$15,000	$7,500	$22,500
Gross margin	$ 5,000	($1,500)	$ 3,500

This statement reveals a loss of $1,500 on product Y. Is that important? Yes, any loss is important. However, the firm must realize that overall it earned a $3,500 profit on the two items in the line. Also, weight may not be the right way to allocate the joint costs. Instead, the firm might use other bases, including market value or quantity sold.

REVIEW LEARNING OUTCOME

LO4 Discuss product line pricing





LO5 Pricing during Difficult Economic Times

Pricing is always an important aspect of marketing, but it is especially crucial in times of inflation and recession. The firm that does not adjust to economic trends may lose ground that it can never make up.

INFLATION

When the economy is characterized by high inflation, special pricing tactics are often necessary. They can be subdivided into cost-oriented and demand-oriented **tactics.**

Cost-Oriented Tactics

One popular cost-oriented tactic is *culling products with a low profit margin* from the product line. However, this tactic may backfire for three reasons:

delayed-quotation pricing A price tactic used for industrial installations and many accessory items, in which a firm price is not set until the item is either finished or delivered.

escalator pricing A price tactic in which the final selling price reflects cost increases incurred between the time the order is placed and the time delivery is made.

- A high volume of sales on an item with a low profit margin may still make the item highly profitable.
- Eliminating a product from a product line may reduce economies of scale, thereby lowering the margins on other items.
- Eliminating the product may affect the price-quality image of the entire line.

Another popular cost-oriented tactic is delayed-quotation pricing, which is used for industrial installations and many accessory items. Price is not set on the product until the item is either finished or delivered. Long production lead times force many firms to adopt this policy during periods of inflation. Builders of nuclear power plants, ships, airports, and office towers sometimes use delayed-quotation tactics. Escalator pricing is similar to delayed-quotation pricing in that the final selling price reflects cost increases incurred between the time an order is placed and the time delivery is made. An escalator clause allows for price increases (usually across the board) based on the cost of living index or some other formula. As with any price increase, management's ability to implement such a policy is based on inelastic demand for the product. About a third of all industrial product manufacturers now use escalator clauses. Many companies do not apply the clause

in every sale, however. Often it is used only for extremely complex products that take a long time to produce or with new customers.

Another tactic growing in popularity is to hold prices constant but add new fees. Take the telecommunications industry, for instance. There are setup fees, change-of-service fees, service-termination fees, directory-assistance fees, regulatory assessment fees, number-portability fees, and cable hookup and equipment fees. Telecom and cable companies have been adding on numerous extra charges to boost revenues and cover expenses. All told, fees add 20 percent to the cost of wireless service, 15 percent to the cost of long distance, and at least 5 percent to cable and satellite service.[29] Financial services firms, airlines, and the travel industry are also notorious for adding on fees. American Airlines, for example, recently added a $350 fee (each way) to use your miles to upgrade to the next class of service on travel to Europe. Like all airlines, American has added many new fees for luggage, fuel charges, and so forth.

price shading
The use of discounts by salespeople to increase demand for one or more products in a line.

Any cost-oriented pricing policy that tries to maintain a fixed gross margin under all conditions can lead to a vicious cycle. For example, a price increase will result in decreased demand, which in turn increases production costs (because of lost economies of scale). Increased production costs require a further price increase, leading to further diminished demand, and so on.

Demand-Oriented Tactics

Demand-oriented pricing tactics use price to reflect changing patterns of demand caused by inflation or high interest rates. Cost changes are considered, of course, but mostly in the context of how increased prices will affect demand.

Price shading is the use of discounts by salespeople to increase demand for one or more products in a line. Often shading becomes habitual and is done routinely without much forethought. Ducommun, a metals producer, is among the major companies that have succeeded in eliminating the practice. Ducommun has told its salespeople, “We want no deviation from book price” unless authorized by management.

To make the demand for a good or service more inelastic and to create buyer dependency, a company can use several strategies:

- *Cultivate selective demand:* Marketing managers can target prosperous customers who will pay extra for convenience or service. Neiman Marcus, for example, stresses quality. As a result, the luxury retailer is more lenient with suppliers and their price increases than is Dollar’s Stores, a discounter. In cultivating close relationships with affluent organizational customers, marketing managers should avoid putting themselves at the mercy of a dominant firm. They can more easily raise prices when an account is readily replaceable. Finally, in companies where engineers exert more influence than purchasing departments do, performance is favored over price. Often a preferred vendor’s pricing range expands if other suppliers prove technically unsatisfactory.
- *Create unique offerings:* Marketing managers should study buyers’ needs. If the seller can design distinctive goods or services uniquely fitting buyers’ activities, equipment, and procedures, a mutually beneficial relationship will evolve. Buyers would incur high changeover costs in switching to another supplier. By satisfying targeted buyers in a superior way, marketing managers can make them dependent. Cereal manufacturers have skirted around passing on costs by marketing unique value-added or multi-ingredient cereals, increasing the perceived quality of cereals and allowing companies to raise prices. These cereals include General Mills’ Basic 4, Clusters, and Oatmeal Crisp; Post’s Banana Nut Crunch and Blueberry Morning; and Kellogg’s Mueslix, Nutri-Grain, and Temptations.

PR NEWSFOTO/© KELLOGG COMPANY

Kellogg is no stranger to creating unique offerings to stimulate demand. It has extended many of its brands by creating cereal bars based on popular boxed cereals, and it has created new, boxed cereals designed to appeal to a variety of markets. One new cereal is Smorz. To create demand for Smorz, Kellogg hosted a summer kickoff event with one hundred thirdgraders, who participated in a S’mores-making contest.

PR NEWSFOTO/© OWENS CORNING

- *Change the package design:* Another way companies pass on higher costs is to shrink product sizes but keep prices the same. Scott Paper Company reduced the number of sheets in the smallest roll of Scott Clean paper towels from 96 to 60 and actually lowered the price by 10 cents a roll. The increases in costs for paper towels were tied to a 50 to 60 percent increase in the cost of pulp paper. The company also changed the names of the sizes to de-emphasize the magnitude of the rolls.
- *Heighten buyer dependence:* Owens-Corning Fiberglass supplies an integrated insulation service (from feasibility studies to installation) that includes commercial and scientific training for distributors and seminars for end users. This practice freezes out competition and supports higher prices.
- *Make strong promotional claims and avoid discounting:* Recent research has found that strong product claims can create greater satisfaction and benefit for consumers. Consumers who were exposed to strong advertising claims about an energy drink's benefits could actually solve more puzzles. (The researchers used individuals' ability to solve puzzles to test the product's benefits.) Persons who bought the same energy drink, but at a discounted price, solved fewer puzzles. Thus, strong benefit promotions and paying full price may actually increase long run demand, according to this research.[30]

RECESSION

A recession is a period of reduced economic activity. Reduced demand for goods and services, along with higher rates of unemployment, is a common trait of a recession. Yet astute marketers can often find opportunity during recessions. A recession is an excellent time to build market share because competitors are struggling to make ends meet.

Two effective pricing tactics to hold or build market share during a recession are value-based pricing and bundling. *Value-based pricing,* discussed earlier in the chapter, stresses to customers that they are getting a good value for their money. Charles of the Ritz, usually known for its pricey products, introduced the Express Bar during a recession. A collection of affordable cosmetics and skin treatment products, the Express Bar sold alongside regular Ritz products in department stores. Although lower-priced products offer lower profit margins, Ritz found that increases in volume can offset slimmer margins. For example, the company found that consumers will buy two or three Express Bar lipsticks at a time.

Bundling or *unbundling* can also stimulate demand during a recession. If features are added to a bundle, consumers may perceive the offering as having greater value. For example, suppose that Hyatt offers a "great escape" weekend for $119. The package includes two nights' lodging and a continental breakfast. Hyatt could add a massage and a dinner for two to create more value for this price. Conversely, companies can unbundle offerings and lower base prices to stimulate demand. A furniture store, for example, could start charging separately for design consultation, delivery, credit, setup, and hauling away old furniture.

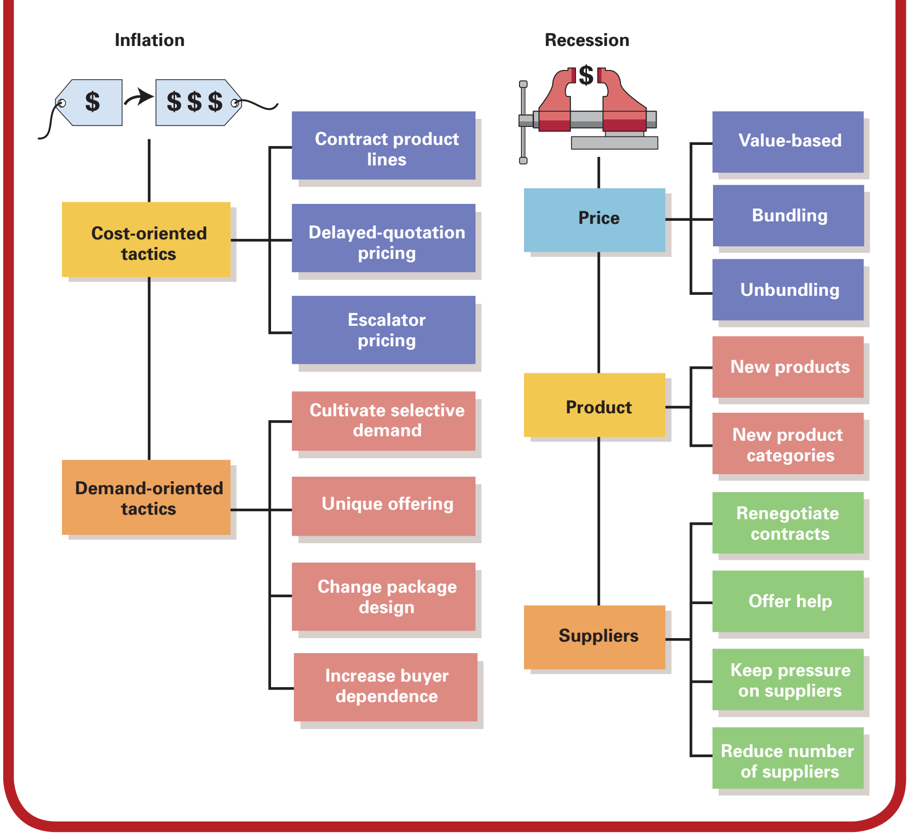
Recessions are a good time for marketing managers to study the demand for individual items in a product line and the revenue they produce. Pruning unprofitable items can save resources to be better used elsewhere. Borden's, for example, found that it made about 3,200 sizes, brands, types, and flavors of snacks—but got 95 percent of its revenues from just half of them.

Prices for fresh and frozen pork fell in the early 2000s, yet Hormel was able to increase both its sales and its profits. The company accomplished this by creating a whole new class of products. Hormel is increasingly turning its low-margin fresh pork—slabs that groceries and restaurants butcher themselves—into highly profitable heat-and-serve meals. These precut, value-added products, such as teriyaki-flavored loins, are easier for consumers to cook. Busy families were avoiding pork because they were not sure how to cook it properly. Grocers, eager to win business back from takeout restaurants, cleared refrigerator space eagerly.

Prices often fall during a recession as competitors try desperately to maintain demand for their wares. Even if demand remains constant, falling prices mean lower profits or no profits. Falling prices, therefore, are a natural incentive to lower costs. During the dot-com recession of the early 2000's, companies implemented new technology to improve efficiency and then slashed payrolls. They also discovered that suppliers were an excellent source of cost savings; the cost of purchased materials accounts for slightly more than half of most U.S. manufacturers' expenses. General Electric's appliance division told 300 key suppliers that they had to reduce prices 10 percent or risk losing GE's business. Honeywell, Dow Chemical, and DuPont made similar demands of their suppliers. Specific strategies that companies use with suppliers include the following:

REVIEW LEARNING OUTCOME

LO5 Describe the role of pricing during periods of inflation and recession



- *Renegotiating contracts:* Sending suppliers letters demanding price cuts of 5 percent or more; putting out for rebid the contracts of those that refuse to cut costs.
- *Offering help:* Dispatching teams of experts to suppliers' plants to help reorganize and suggest other productivity-boosting changes; working with suppliers to make parts simpler and cheaper to produce.
- *Keeping the pressure on:* To make sure that improvements continue, setting annual, across-the-board cost reduction targets, often of 5 percent or more a year.
- *Paring down suppliers:* To improve economies of scale, slashing the overall number of suppliers, sometimes by up to 80 percent, and boosting purchases from those that remain.

Tough tactics like these help keep companies afloat during economic downturns.

percentage of companies who conduct serious pricing research > **8**

88 < percentage of companies who do little or no pricing research

cost of a year's supply of Ceredase to treat one patient with Gaucher's disease > **$300,000**

$50 < cost of a typical electric toothbrush

cost of Crest SpinBrush > **$5**

85 < percentage of U.S. vitamin C manufactured in China

percentage of rebates that are never redeemed > **40**

square feet in a One Price Clothing Store > **3,000**

84 < percentage of the likelihood that theater season ticket purchasers will attend the first play

percentage of the likelihood that theater season ticket purchasers will attend any given play > **78**

Review and Applications

LO 1

Describe the procedure for setting the right price. The process of setting the right price on a product involves four major steps: (1) establishing pricing goals; (2) estimating demand, costs, and profits; (3) choosing a price policy to help determine a base price; and (4) fine-tuning the base price with pricing tactics.

A price strategy establishes a long-term pricing framework for a good or service. The three main types of price policies are price skimming, penetration pricing, and status quo pricing. A price-skimming policy charges a high introductory price, often followed by a gradual reduction. Penetration pricing offers a low introductory price to capture a large market share and attain economies of scale. Finally, status quo pricing strives to match competitors' price.

1.1 A manufacturer of office furniture decides to produce antique-style rolltop desks reconfigured to accommodate personal computers. The desks will have built-in surge protectors, a platform for raising or lowering the monitor, and a number of other features. The high-quality, solid-oak desks will be priced far below comparable products. The marketing manager says, "We'll charge a low price and plan on a high volume to reduce our risks." Comment.

1.2 Janet Oliver, owner of a mid-priced dress shop, notes, "My pricing objectives are simple: I just charge what my competitors charge. I'm happy because I'm making money." React to Janet's statement.

1.3 What is the difference between a price policy and a price tactic? Give an example.

LO 2

Identify the legal and ethical constraints on pricing decisions. Government regulation helps monitor four major areas of pricing: unfair trade practices, price fixing, resales price maintenance, predatory pricing and predatory bidding, and price discrimination. Many states have enacted unfair trade practice acts that protect small businesses from large firms that operate efficiently on extremely thin profit margins; the acts prohibit charging below-cost prices. The Sherman Act and the Federal Trade Commission Act prohibit both price fixing, which is an agreement between two or more firms on a particular price, and predatory pricing, in which a firm undercuts its competitors with extremely low prices to drive them out of business. Finally, the Robinson-Patman Act makes it illegal for firms to discriminate in price between two or more buyers who purchase like grade and quantity goods.

2.1 What are the three basic defenses that a seller can use if accused under the Robinson-Patman Act?

LO 3

Explain how discounts, geographic pricing, and other pricing tactics can be used to fine-tune the base price. Several techniques enable marketing managers to adjust prices within a general range in response to changes in competition, government regulation, consumer demand, and promotional and positioning goals. Techniques for fine-tuning a price can be divided into three main categories: discounts, allowances, rebates, and value-based pricing; geographic pricing; and other pricing tactics.

The first type of tactic gives lower prices to those that pay promptly, order a large quantity, or perform some function for the manufacturer. Value-based pricing starts with the customer, considers the competition and costs, and then determines a price. Additional tactics in this category include seasonal discounts, promotion allowances, rebates (cash refunds), zero percent financing, and markdown money.

Geographic pricing tactics—such as FOB origin pricing, uniform delivered pricing, zone pricing, freight absorption pricing, and basing-point pricing—are ways of moderating the impact of shipping costs on distant customers.

A variety of "other" pricing tactics stimulate demand for certain products, increase store patronage, and offer more merchandise at specific prices.

More and more customers are paying price penalties, which are extra fees for violating the terms of a purchase contract. The perceived fairness or unfairness of a penalty may affect some consumers' willingness to patronize a business in the future.

WRITING

3.1 You are contemplating a price change for an established product sold by your firm. Write a memo analyzing the factors you need to consider in your decision.

3.2 Columnist Dave Barry jokes that federal law requires this message under the sticker price of new cars: "Warning to stupid people: Do not pay this amount." Discuss why the sticker price is generally higher than the actual selling price of a car. Tell how you think car dealers set the actual prices of the cars they sell.

TEAM

3.3 Divide into teams of four persons. Each team should choose one of the following topics: skimming, penetration pricing, status quo pricing, price fixing, geographic pricing, adopting a single-price tactic, flexible pricing, or professional services pricing. Each team should then pick a retailer that it feels most closely follows the team's chosen pricing strategy. Go to the store and write down examples of the strategy. Interview the store manager and get his or her views on the advantages and disadvantages of the strategy. Each team should then make an oral report in class.

3.4 The U.S. Postal Service regularly raises the price of a first-class stamp but continues to operate in the red year after year. Is uniform delivered pricing the best choice for first-class mail? Explain your reasoning.

3.5 How is the "information age" changing the nature of pricing?

3.6 Have you ever paid a price penalty? How did it affect your attitude toward that company?

WRITING

3.7 Imagine that you are a marketing manager for a mid-sized amusement park. You have attended an industry-wide meeting where a colleague gave a talk about new pricing strategies for amusement parks. You were very motivated by the seminar. On your return to work, write a memo to your boss outlining the pros and cons of the new pricing strategy. End your memo with a recommendation either for or against à la carte pricing of attractions (pricing each attraction separately rather than charging a single high entrance fee).

LO4

Discuss product line pricing. Product line pricing maximizes profits for an entire product line. When setting product line prices, marketing managers determine what type of relationship exists among the products in the line: complementary, substitute, or neutral. Managers also consider joint (shared) costs among products in the same line.

4.1 Develop a price line strategy for each of these firms:

a. a college bookstore

b. a restaurant

c. a video rental firm

LO5

Describe the role of pricing during periods of inflation and recession. Marketing managers employ cost-oriented and demand-oriented tactics during periods of economic inflation. Cost-oriented tactics include dropping products with a low profit margin, using delayed-quotation pricing and escalator pricing, and adding fees. Demand-oriented pricing methods include price shading and increasing demand through cultivating selected customers, creating unique offerings, changing the package size, and heightening buyer dependence.

To stimulate demand during a recession, marketers use value-based pricing, bundling, unbundling, and making strong promotional claims while avoiding discounting. Recessions are also a good time to prune unprofitable items from product lines. Managers strive to cut costs during recessions in order to maintain profits as revenues decline. Implementing new technology, cutting payrolls, and pressuring suppliers for reduced prices are common techniques used to cut costs. Companies also create new value-added products.

5.1 During a recession, what pricing strategies would you consider using to gain or maintain market share? Explain your answer.

ONLINE

5.2 After a decade of astounding growth and prosperity, Americans were challenged by the economic downturn of the early 2000s. As a result, pricing became an issue for many consumers looking to pinch pennies. This was also true in areas where penny-pinching isn't a common occurrence, like high-end retailers. Search *The Wall Street Journal* online archives (**http://www.wsj.com**) to find an article about pricing during a recession.

Key Terms

Exercises

APPLICATION EXERCISE

You read in the chapter about the dangers of pricing products too low. It seems so obviously wrong, but do companies really price their products so low that they won't make any money? After all, companies are in business to make money, and if they don't, they're probably not in business for very long. Let's take a deeper look at the effects of pricing products too low or creating too deep discounts during sale periods.[31]

Activity

1. The average markup for a produce department is 28 percent on selling price. When sold at 28 percent markup on selling price, bananas usually account for 25 percent of department sales and 25 percent of department markup. This week, because bananas were on special sale at the retailer's cost, the department sold twice as many pounds of bananas as usual. However, they were sold at zero markup. If all other things remain the same, what is the average markup on selling price for the entire produce department this week?

ETHICS EXERCISE

ETHICS

People feel better when they think they are getting a great bargain when they shop. Knowing this, some retailers mark up items above the traditional retail price and then offer a 60 percent discount. If they had simply discounted the normal retail price by 20 percent the resulting "sale price" would have been the same. One retailer says that he is just making shoppers happy that they got a great deal when he inflates the retail price before discounting.

Questions

1. What do you think?
2. Does the AMA Statement of Ethics address this issue? Go to **http://www.marketing-power.com** and review the statement. Then, write a brief paragraph summarizing what the AMA Code of Ethics contains that relates to retail pricing.

Case Study: Wal-Mart

HOW LOW CAN DRUG PRICES GO?

When Wal-Mart rolled out its new prescription-drug plan in 2006, lowering the prices on 331 commonly prescribed medications to a flat $4, Frank Ganci's doctor told him to check it out. He has no health insurance and his prescriptions were costing him $110 a month at his local pharmacy, so switching to Wal-Mart meant that he could get the same three medications for $12. Now he says he's a loyal Wal-Mart customer: "If they don't make up the money on prescriptions, they're going to make it up on my clothes and food purchases."

Industry analysts speculate that Wal-Mart is counting on customers like Ganci to spend the money they saved at the pharmacy on other products in the store. Wal-Mart insists that it can earn a profit on the $4 prescriptions alone, however, since more expensive medications are not discounted. "It can only be in our program if it is profitable," says Bill Simon, a Wal-Mart CEO.

It's true that pharmacies can buy some types of generics from manufacturers for less than $4. For example, a month's supply of fluoxetine, the generic version of Prozac, can be obtained for 75 cents. But store overhead and pharmacists' salaries bring the true cost closer to $15. It would be difficult for smaller pharmacies to match the $4 price point, which has some of Wal-Mart's competitors complaining that it violates predatory pricing laws. "You can't just sell something below your cost to drive out the small guy," says Rick Sain, co-owner of a drugstore in Tennessee. "You have to at least set a fair price. That's what all the states that have fair trade laws in place are looking into because you cannot dispense a prescription for $4. They are saying you can."

Wal-Mart later increased the price of certain generic drugs from $4 to $9 in order to bring the company into compliance with all "low-cost laws," according to a company statement. John Rector of the National Community Pharmacists Association says, "We don't know for certain whether it can make a profit on the $4 drugs so they don't violate these laws. But we strongly doubt it, and the fact is [raising some prices] gives us insight into what its business practices are."

Stores like Target and Kmart quickly lowered their own prices to match Wal-Mart's, but Walgreens and CVS both announced that their prices would remain the same. Tony Civello, CEO of Kerr Drug, insists, "We will not treat your prescription like t-shirts and blue jeans. Wal-Mart may choose to use some limited prescription drugs as a loss leader. But our patients' health care is not a loss leader. We will not compromise that."

Bill Vaughan, a policy analyst for Consumers Union, argues that the price slashing is actually step in the right direction. "It's the beginning of better competition in a sector where it's literally pennies per pill," he said. When a generic drug is introduced, pharmacies can charge as much as they like for it. One study found that mark-ups were often as high as 4,000%. Few people compare drug prices from one pharmacy to the next, so pharmacies are able to mark up prices substantially.

Wal-Mart's prescription program seems to be raising consumer awareness as it demonstrates how low the prices of the drugs can go. The discounts are especially welcome among uninsured Americans and seniors living on fixed incomes. Legislators have listened to constituents who rely on the $4 plan and efforts are under way in states like Colorado and Minnesota to either repeal predatory-pricing laws or exempt prescription drugs from them.

The prescriptions in Wal-Mart's $4 program now make up more than 35% of all prescriptions they fill, and the company boasts that the program has saved consumers more than $340 million in drug costs already. Wal-Mart executive H. Lee Scott is enthusiastic about its future, saying, "The $4 prescription program is absolutely one of the coolest things that we have done in a long time."[32]

Questions

1. Do you believe Wal-Mart is engaging in predatory pricing with its $4 generic drug program? Why or why not?
2. Do you think that predatory pricing laws should be amended to exclude prescription drugs? Explain.
3. If you owned a pharmacy next door to a Wal-Mart store, what strategies could you try in order to compete? Would you match their prices if possible, or would you find other ways to add value? What could a small pharmacy like yours offer customers that Wal-Mart's might not?

Company Clips

PRICING PERSPECTIVES – METHOD, READYMADEMAG, SEPHORA, VANS, AND ACID+ALL

Setting the right price is one of the most challenging aspects of a marketer's job. How high a price will the market bear? What kind of message does the price communicate? How flexible can our price be? The answer to those and a multitude of other questions relating to price vary by industry, by product categories within an industry, and even by brand and store.

This video shows you a wide range of pricing issues and concerns facing new brands, like Method, ReadyMadeMag, and Acid+All, and established brands, like Sephora and Vans. There are both similarities and differences in the tools each company uses to set and fine-tune its base price. One idea, however, unifies all of the companies: pricing is a considered strategy, not an afterthought.

Questions

1. Compare the pricing strategies of Method, ReadyMadeMag, and Acid+All. Do all of these relatively new brands use the same strategy? Explain.
2. In what ways is the pricing strategy of Sephora similar to that of Acid+All?
3. Does it make sense for Method to use product line pricing? Why or why not?
4. What is Vans' primary strategy for setting prices on tickets to the Warped Tour it sponsors?

Marketing & You Results

High scores on this poll indicate that you are very sensitive to prices and that your price consciousness affects how you shop. Conversely, a lower score suggests that you are not very price conscious.

Marketing Miscue

Amazon's Pricing Error Hits the Game Blogs

Headquartered in Seattle, Washington (USA), Amazon.com is one of the most prominent online retailers. With retail websites such as www.amazon.com, www.amazon.ca, www.amazon.de, www.amazon.fr, www.amazon.co.jp, www.amazon.co.uk, www.joyo.com, www.shopbop.com, and www.endless.com, the company is truly a worldwide provider of services. The company offers products in the following categories: books; movies, music & games; digital downloads; electronics & computers; home & garden; grocery; toys, kids & baby; apparel, shoes & jewelry; health & beauty; sports & outdoors; and tools, auto & industrial.

Within the movies, music & games product category is the video game section of Amazon's retail offerings. The company offers video games for major consoles such as PlayStation 3, PlayStation 2, Xbox 360, Xbox, Wii, and GameCube, as well as for a wide variety of other consoles, computer, and handheld systems. Recently, **www.amazon.co.uk** was a popular site for ordering the *Lair* and *Folklore* games for the PS3.

Lair is a video game in the action genre featuring a warrior riding a voracious dragon. The goal is for the gamer, playing as the warrior, and the dragon to destroy enemies and save the world from destruction. Published by Sony Computer Entertainment and developed by Factor 5, the manufacturer's suggested retail price (MSRP) was $59.99. *Folklore*, developed by Game Republic and published by Sony Computer Entertainment, falls in the adventure genre where the action takes place in a community in which the living can meet the dead. The manufacturer's suggested retail price (MSRP) for *Folklore* was also $59.99. Both games were released in the fall of 2007.

Gamer blogs were inundated in late August of 2007 with notices of the game deal that Amazon.com.uk was offering on these two games. Apparently, the online retailer was offering these two games for £14.95 each, less than half the MSRP. The flurry of excitement surrounding the offerings at this price resulted in pre-orders that drove both games to the top of the bestselling list. At one point, *Lair* and *Folklore* were listed as numbers one and two respectfully on the site's most popular items in the PC & Video Game category.

Some consumers went so far as to contact Amazon UK and ask if there was a pricing mistake. Game bloggers reported that the company responded with an e-mail stating that the orders for *Lair* and *Folklore* were confirmed at a price of £14.95 each. Purportedly, the Amazon e-mail said that the company would honor the prices given at the time of order placement and that there would not be any changes to the price of the items. However, less than 24 hours after purchasers reported receiving this e-mail honoring the listed prices, the game blogs were inundated with reports that Amazon UK had cancelled pre-orders for the games at the £14.95 prices. The company was reporting that there was a mistake in the recording of prices and that pre-orders had to be cancelled. According to the follow-up e-mail sent by Amazon UK, it was standard operating procedure to cancel orders when the reported price was lower than the actual retail price. Purchasers still interested in pre-ordering these two games were instructed to place a new online order.

To its credit, Amazon's pricing policy is explained clearly on its website. In addition to providing information with respect to list pricing and third-party sellers, the company states, "Despite our best efforts, a small number of items in our catalog may be mispriced. If an item's correct price is higher than our stated price, we will, at our discretion, either contact you for instructions before shipping or cancel your order and notify you of such cancellation." However, gamers were surprised that the company was rescinding its earlier e-mail in which it had said that it would honor the originally noted price.

At the end of 2007, Amazon's video game editors released a list of the overall Top Ten games for 2007, as well as the best 10 games for each platform. Interestingly, while *Liar* and *Folklore* were numbers one and two in August of 2007 due to the pre-orders, neither of them made it to the most popular games listings for the year.

Questions:

1. What is the relationship between demand and price for video games?
2. Should there be retailer penalties, similar to consumer penalties, for violating terms of sale in instances such as this?
3. If you had made an initial purchase of Lair or Folklore and then found the price rescinded would you continue to shop with **Amazon.com.uk**? Why?

PR NEWSFOTO/© NINTENDO

Critical Thinking Case

Lenovo's Asia-Pacific Pricing

In late summer of 2007, Lenovo Group Ltd. announced some interesting product and pricing decisions related to its personal computer lines in the Asia-Pacific region. In particular, the company publicized its decision to offer a $199 basic personal computer in China's rural market and another decision to offer a $1,000 Power Rangers Mystic Force themed desktop computer to children in India.

Lenovo offers a full range of personal computer products and accessories, including notebook and desktop computers, mobile handsets, and software, as well as services for small, medium, and large businesses. The company is headquartered in Raleigh, North Carolina, and employs around 25,000 people. In an impressive drive for growth, Lenovo, the leading personal computer producer in China, bought the personal computer division of IBM for $1.75 billion in late 2004. The purchase moved Lenovo to the number three industry spot behind Dell and Hewlett-Packard.

Online in China and India

It is estimated that there are close to 140 million Internet users in China, which places China second only to the United States in terms of Internet usage. The Chinese government seems wary of the Internet and often censors Web sites. The current Internet user in China is typically a male student (under 30 years of age) in an urban setting. Geographically, the Internet penetration rate is around 20 percent in the urban areas and three percent in rural areas. Around 70 percent of the Chinese population (approximately 800 million) resides in the rural countryside, with an average income of 4,200 yuan ($560) a year. Chinese farmers account for only 0.4 percent of the online population, although valuable farm-related information, such as weather forecasts and product prices, would facilitate productivity. Expectations are that the new wave of users will be from the rural areas.

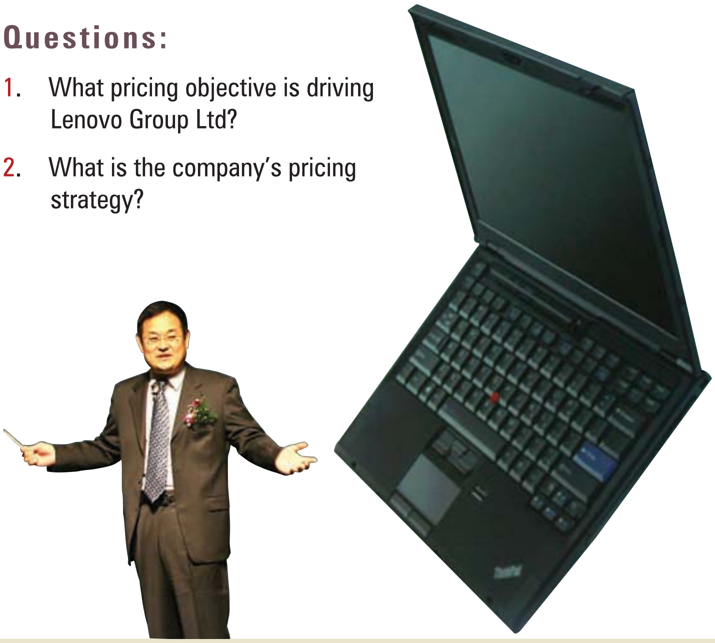
The population of India is around 1.1 billion, with around 37 million Indians denoted as users of the Internet. Around 60 percent of these users access the Internet from public Internet cafes, while the installed base of personal computers is only around 20 million. This installed base accounts for installations in homes, businesses and governmental and educational institutions. While Internet usage was expected to grow 160 percent between 2006 and 2008, India still lags in online usage.

The Products and Prices

- The Lenovo personal computer to be introduced in rural China will be marketed to parents as an educational tool for their children. Hopefully, children in these rural areas will learn to use computers just like the Chinese children living in the wealthy coastal cities of the country. The computer will sell for 1,499 to 2,999 yuan ($199-$399) and will include a processor and keyboard. The system utilizes the buyer's television set as a monitor and is expected to come pre-loaded with agricultural software. Lenovo plans to set up a rural sales network of 5,000 dealers to reach potential customers. The company does not plan to sell this low-priced personal computer outside of China.
- Disney's Power Rangers are among the most popular action adventure series in the world, becoming extremely popular among the Indian audience. The series is viewed on JETIX in India. Related merchandising, on-air contests, mobile gaming, and live events have also proved to be very successful for the station. Lenovo and Disney Consumer Products partnered to release the Lenovo 3000H limited edition Power Ranger desktop in India. Prices will start at 40,100 Indian rupees (around $935). The desktop comes with a 17" LCD monitor, 1GB RAM, built-in modem, optical mouse, and Power Ranger speakers. It is preloaded with Microsoft Vista Home Basic edition. Via a phased rollout, the limited edition Power Rangers Mystic Force themed desktop will be introduced first in Mumbai, Lucknow, Calcutta, Bangalore, Chandigarh, and Delhi. A national rollout will follow in the second phase. The computer will be sold in Lenovo-authorized storefronts.

Questions:

1. What pricing objective is driving Lenovo Group Ltd?
2. What is the company's pricing strategy?



ANATOMY OF Product Line Pricing

McDonald's menu…

There would probably be little demand for a menu item that was out of the price/value range established by other items in McDonald's product line. For example, a $10 burger would be well out of the price range that McDonald's customers expect for that product class.

1 …offers several related products.

2 …sells related products individually and in combinations.

3 …offers a line of products of various sizes, qualities, and prices.

4 …presents a limited number of prices for all their product offerings.

What would you pay for a fast-food burger:

$1, $2, $3, ~~$10~~ ?

PART 7

Technology-Driven Marketing

WHAT'S INSIDE

CHAPTER 21 Customer Relationship Management (CRM)

Learning Outcomes

LO 1 Define customer relationship management

LO 2 Explain how to identify customer relationships with the organization

LO 3 Understand interactions with the current customer base

LO 4 Outline the process of capturing customer data

LO 5 Describe the use of technology to store and integrate customer data

LO 6 Describe how to identify the best customers

LO 7 Explain the process of leveraging customer information throughout the organization

LO 1

What Is Customer Relationship Management?

Customer relationship management (CRM) is the ultimate goal of a new trend in marketing that focuses on understanding customers as individuals instead of as part of a group. To do so, marketers are making their communications more customer-specific, like the personalized marketing efforts being used by Amazon.com. This movement initially was popularized as one-to-one marketing. But CRM is a much broader approach to understanding and serving customer needs than is one-to-one marketing.

customer relationship management (CRM) A company-wide business strategy designed to optimize profitability, revenue, and customer satisfaction by focusing on highly defined and precise customer groups.

Customer relationship management is a company-wide business strategy designed to optimize profitability, revenue, and customer satisfaction by focusing on highly defined and precise customer groups. This is accomplished by organizing the company around customer segments, establishing and tracking customer interactions with the company, fostering customer-satisfying behaviors, and linking all processes of the company from its customers through its suppliers. For example, Listen.com's Rhapsody player targets consumers who listen to streaming audio. Then, by requiring users to log in, Rhapsody tracks their musical preferences and usage. Listen.com can leverage this information to offer special promotions and make recommendations to specific target markets and individuals.

The difference between CRM and traditional mass marketing can be compared to shooting a rifle and a shotgun. If you have good aim, a rifle is the more efficient weapon to use. A shotgun, on the other hand, increases your odds of hitting the target when it is more difficult to focus. Instead of scattering messages far and wide across the spectrum of mass media (the shotgun approach), CRM marketers now are homing in on ways to effectively communicate with each individual customer (the rifle approach).

THE CUSTOMER RELATIONSHIP MANAGEMENT CYCLE

On the surface, CRM may appear to be a rather simplistic customer service strategy. But, though customer service is part of the CRM process, it is only a small part of a totally integrated approach to building customer relationships. CRM is often described as a closed-loop system that builds relationships with customers. Exhibit 21.1 illustrates this closed-loop system, one that is continuous and circular with no predefined starting or end point.[1]

To initiate the CRM cycle, a company must first *identify customer relationships with the organization*. This may simply entail learning who the customers are or where they are located, or it may require more detailed information on the products and services they are using. Bridgestone/Firestone, a tire manufacturer and tire service company, uses a CRM system called OnDemand5.[2] OnDemand5 initially

Marketing & You

How do you feel about complaining? Enter your answers on the lines provided.

1	2	3	4	5	6
Strongly agree		Agree	Disagree		Strongly disagree

— People are bound to end up with an unsatisfactory product once in a while, so they shouldn't complain to the store or the manufacturer about it.*

— It bothers me quite a bit if I don't complain about an unsatisfactory product.

— It sometimes feels good to get my dissatisfaction and frustration with a product off my chest by complaining.

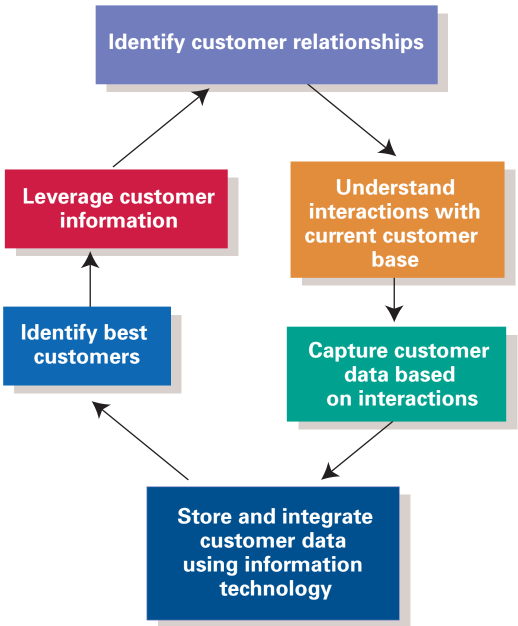
— I often complain when I'm dissatisfied with a business or a product because I feel it is my duty to do so.

— I don't like people who complain to stores because usually their complaints are unreasonable.*

Now, total your score, reversing your answers for the items followed by an asterisk (for example, if you answered 3, enter 4). Find out what your score means after reading the chapter.

Exhibit 21.1

A Simple Flow Model of the Customer Relationship Management System



COURTESY, ©FEDEX

gathers information from a point-of-sale interaction. The types of information gathered include basic demographic information, how frequently consumers purchase goods, how much they purchase, and how far they drive.

Next, the company must *understand the interactions with current customers*. Companies accomplish this by collecting data on all types of communications a customer has with the company. Using its OnDemand5 system, Bridgestone/Firestone can add information based on additional interactions with the consumer such as multiple visits to a physical store location and purchasing history. In this phase, companies build on the initial information collected and develop a more useful database.

Using this knowledge of its customers and their interactions, the company then *captures relevant customer data on interactions*. As an example, Bridgestone/Firestone can collect such relevant information as the date of the last communication with a customer, how often the customer makes purchases, and whether the customer redeemed coupons sent through direct mail.

How can marketers realistically analyze and communicate with individual customers? How can huge corporations like FedEx and Williams-Sonoma manage relationships with each and every one of their millions of customers on a personal level? The answer lies in how information technology is used to implement the CRM system. Fundamentally, a CRM approach is no more than the relationship cultivated by a salesperson with the customer. A successful salesperson builds a relationship over time, constantly thinks about what the customer needs and wants, and is mindful of the trends and patterns in the customer's purchase history. A good salesperson often knows what the customer needs even before the customer knows. The salesperson may also inform, educate, and instruct the customer about new products, technology, or applications in anticipation of the customer's future needs or requirements.

This kind of thoughtful attention is the basis of successful CRM systems. Information technology is used not only to enhance the collection of customer data, but also to *store and integrate customer data* throughout the company and, ultimately, to "get to know" customers on a personal basis. Customer data are the firsthand responses that are obtained from customers through investigation or by asking direct questions. These initial data, which might include individual answers to questionnaires, responses on warranty cards, or lists of purchases recorded by electronic cash registers, have not yet been analyzed or interpreted.

The value of customer data depends on the system that stores the data and the consistency and accuracy of the data captured. Obtaining high-quality, actionable data from various sources is a key element in any CRM system. Bridgestone/Firestone accomplishes this by managing all information in a central database accessible by marketers. Different kinds of database management software are available, from extremely high-tech, expensive, custom-designed databases to standardized programs. Oracle, the world's largest CRM software company, offers customized software for any type of CRM application. In contrast, NetERP offers users database software in a standardized format that is available at a much lower cost.[3]

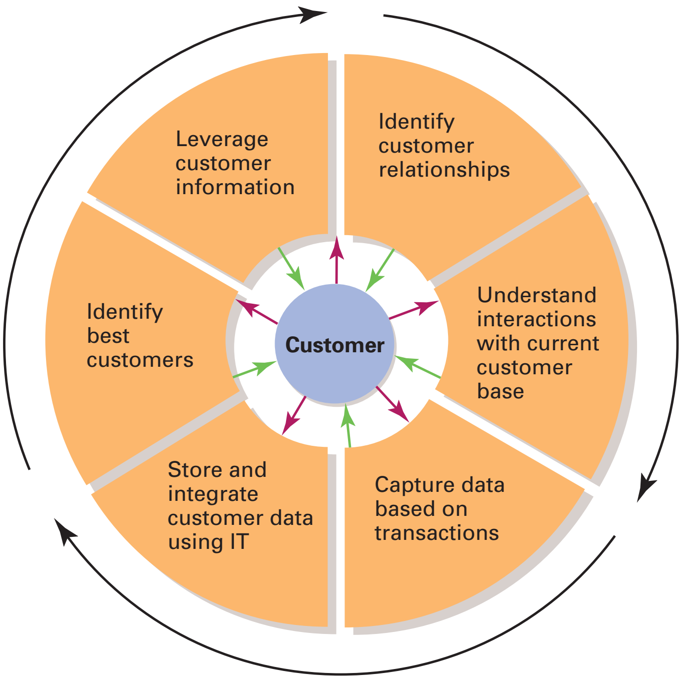
Every customer wants to be a company's main priority. Yet not all customers are equally important in the eyes of a business. Some customers are simply more profitable for the company than others. Consequently, the company must identify *its profitable and unprofitable customers*. Data mining is an analytical process that compiles actionable data about the purchase habits of a firm's current and potential customers. Essentially, data mining transforms customer data into customer information a company can use to make managerial decisions. The NetERP software enables managers to customize their "dashboard" to obtain real-time reports on top-selling items and gross sales over a given time period. Similarly, Bridgestone/Firestone uses OnDemand5 to analyze its data to determine which customers qualify for the MasterCare Select program. It also identifies customers who have not made a purchase in the past 8 to 12 months.

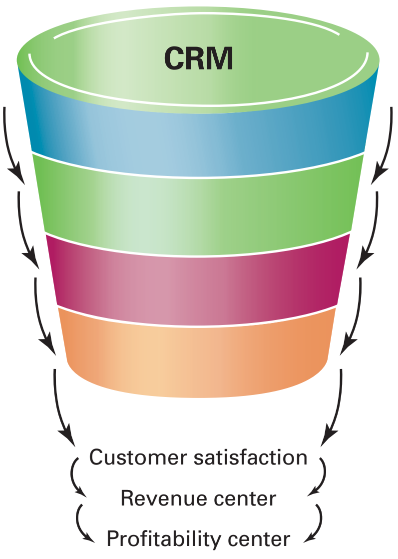
Once customer data are analyzed and transformed into usable information, the information must be *leveraged*. The CRM system sends the customer information to all areas of a business because the customer interacts with all aspects of the business (e.g., sales or marketing, operations, production, accounting). Essentially, the company is trying to enhance customer relationships by getting the right information to the right person in the right place at the right time.

Bridgestone/Firestone utilizes the information in its database to develop different marketing campaigns for each type of customer. For example, MasterCare Select customers receive free tire rotation, maps, roadside assistance, and lost-key service. Customers are also targeted by promotions aimed at increasing store visits, upgrades to higher-end tires, and purchases of additional services. Since the company customized its mailings to each type of customer, visits to stores have increased by more than 50 percent.[4]

REVIEW LEARNING OUTCOME

LO 1 Define customer relationship management





IMPLEMENTING A CUSTOMER RELATIONSHIP MANAGEMENT SYSTEM

Our discussion of a CRM system has assumed two key points. First, customers take center stage in any organization. Second, the business must manage the customer relationship across all points of customer contact throughout the entire organization. The Seattle Mariners baseball team took proactive steps to increase customer attendance at games based on these two points. The team implemented a loyalty card program to help the Mariners "better understand the fans." By collecting information from every interaction a customer has with the Mariners, from visiting concession stands to purchasing online tickets and even frequenting retail stores that sell Mariner merchandise, marketers were able to track the number of games consumers were attending. They sent reminder e-mails if a fan was close to achieving "season-ticket holder" status, and they also monitored complaints. For example, when the CRM system identified a complaint from a fan about the smell of garlic fries, the organization moved the fan to an area where there were no frequent consumers of garlic fries.[5]

In the next sections, we examine how a CRM system is implemented and follow the progression depicted in Exhibit 21.1 as we explain each step in greater detail.

LO 2

Identify Customer Relationships

© AP PHOTO

Sony's PlayStation system is one of the leaders in the video game market. To increase customer loyalty and ensure that the company's products meet the needs and wants of its target market, Sony designed a Web site that feels like an exclusive club for video gamers. And through player feedback, Sony can refine its site to match its customers' exact wants as they evolve.

Companies that have a CRM system follow a customer-centric focus or model. Customer-centric is an internal management philosophy similar to the marketing concept discussed in Chapter 1. Under this philosophy, the company customizes its product and service offering based on data generated through interactions between the customer and the company. This philosophy transcends all functional areas of the business (production, operations, accounting, etc.), producing an internal system where all of the company's decisions and actions are a direct result of customer information.

A customer-centric company builds long-lasting relationships by focusing on what satisfies and retains valuable customers. For example, Sony's Web site (**http://www.playstation.com**) focuses on learning, customer knowledge management, and empowerment to market its PlayStation gaming computer entertainment system. The PlayStation Web site is designed to create a community of users who can join PlayStation Underground where they will "feel like they belong to a subculture of intense gamers." To achieve this objective, the Web site offers online shopping, opportunities to try new games, customer support, and information on news, events, and promotions. The interactive features include online gaming and message boards.

The PlayStation is designed to support Sony's CRM system. When PlayStation users want to access amenities on the site, they are required to log in and supply information such as their name, e-mail address, and birth date. Users can opt to fill out a survey that asks questions about the types of computer entertainment systems they own, how many games are owned for each console, expected future game purchases, time spent playing games, types of games played, and level of Internet connectivity. Armed with this information, Sony marketers are then able to tailor the site, new games, and PlayStation hardware based on players' replies to the survey and use of the Web site.[6]

Customer-centric companies continually learn ways to enhance their product and service offerings. Learning in a CRM environment involves collecting customer information through comments and feedback on product and service performance. As just described, Sony uses its PlayStation Web site to gather information from surveys and message boards so that it can offer more customer-friendly products and services.

Each unit of a business typically has its own way of recording what it learns and perhaps even its own customer information system. The departments' different interests make it difficult to pull all of the customer information together in one place using a common format. To overcome this problem, companies using CRM rely on knowledge management. Knowledge management is a process by which customer information is centralized and shared in order to enhance the relationship between customers and the organization. Information collected includes experiential observations, comments, customer actions, and

customer-centric
A philosophy under which the company customizes its product and service offering based on data generated through interactions between the customer and the company

empowerment
Delegation of authority to solve customers' problems quickly—usually by the first person that the customer notifies regarding the problem.

learning
An informal process of collecting customer data through customer comments and feedback on product or service performance.

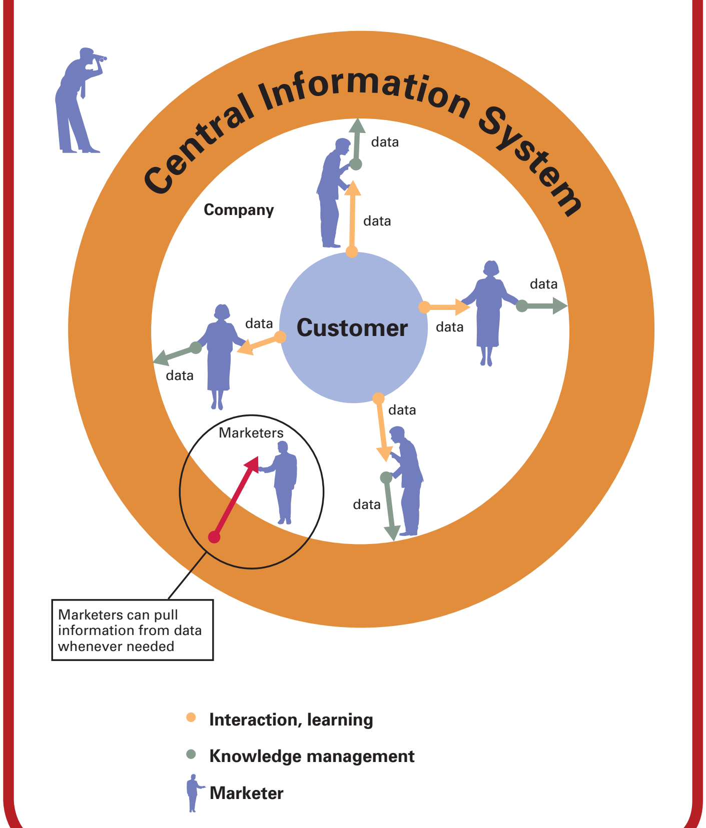
knowledge management
The process by which learned information from customers is centralized and shared in order to enhance the relationship between customers and the organization.

interaction
The point at which a customer and a company representative exchange information and develop learning relationships.

qualitative facts about the customer. For example, PlayStation marketers gather survey information and generate a computer file for each customer that is available to the call center as well as on the Web site. If a PlayStation user registers and purchases a yellow console but then wants to change to a silver console, he or she can call the customer service line, and the representative on the other end will change the order and indicate its availability.[7]

REVIEW LEARNING OUTCOME

LO 2 Explain how to identify customer relationships with the organization



An **interaction** is a touch point at which a customer and a company representative exchange information and develop learning relationships. With CRM, the customer, and not the organization, defines the terms of the interaction, often by stating his or her preferences. The organization responds by designing products and services around customers' desired experiences. For example, students can purchase the Student Advantage Discount Card for a nominal fee and use it to obtain discounts from affiliated retailers, such as Dell, Foot Locker, Target, Timberland, and Barnes & Noble. Student Advantage tracks the cardholders' spending patterns and behaviors to gain a better understanding of what the college customer wants. Student Advantage then communicates this information to the affiliated retailers, who can tailor their discounts to meet college students' needs. Ultimately, everyone benefits from this program: cardholders get relevant discounts, and retailers enjoy increased sales.[8]

The success of CRM—building lasting and profitable relationships—can be directly measured by the effectiveness of the interaction between the customer and the organization. In fact, what further differentiates CRM from other strategic initiatives is the organization's ability to establish and manage interactions with its current customer base. The more latitude (empowerment) a company gives its representatives, the more likely the interaction will conclude in a way that satisfies the customer.

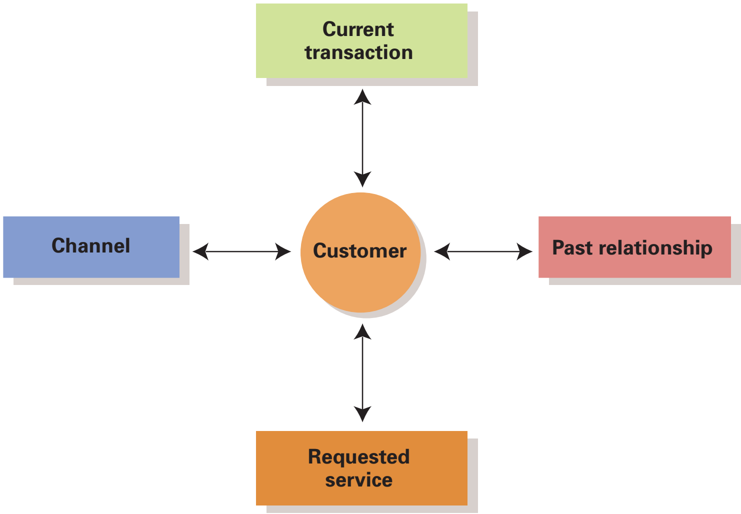
LO 3
Understand Interactions of the Current Customer Base

The *interaction* between the customer and the organization is the foundation on which a CRM system is built. Only through effective interactions can organizations learn about the expectations of their customers, generate and manage knowledge about them, negotiate mutually satisfying commitments, and build long-term relationships.

Exhibit 21.2 illustrates the customer-centric approach for managing customer interactions. Following a customer-centric approach, an interaction can occur through a formal or direct communication channel, such as a phone, the Internet, or a salesperson. Interactions also occur through a previous relationship a customer has had with the organization, such as a past purchase or a survey response, or through some current transaction or request by the customer, such as an actual

Exhibit 21.2

Customer-Centric Approach for Managing Customer Interactions



product purchase, a request for repair service, or a response to a coupon offer. In short, any activity or touch point a customer has with an organization, either directly or indirectly, constitutes an interaction.

Best Buy, an electronic retail superstore, offers a Performance Service Plan (PSP) on products bought in-store or online. The PSP guarantees products against damage and malfunctioning. If customers need assistance, they can contact the company by mail, phone, in-store, or online. All initial purchase contact information is kept in the customer database, along with copies of the PSP. If a customer calls the Customer Care 1-800 number, the representative will have access to all of this information and can either help the customer or refer him or her to another representative. Thus, any form of communication with Best Buy, whether initiated by the customer or by a company representative, qualifies as an interaction or touch point.[9]

touch points
All possible areas of a business where customers communicate with that business.

Companies that effectively manage customer interactions recognize that customers provide data to the organization that affect a wide variety of touch points. In a CRM system, **touch points** are all areas of business where customers have contact with the company, either personally or virtually, and data can be collected. Touch points might include a customer registering for a particular service, a customer communicating with customer service for product information, a customer completing and returning the warranty information card for a product, or a customer talking with salespeople, delivery personnel, and product installers. In the Best Buy example, touch points include the initial customer-initiated purchase and the customer-initiated call to the Customer Care line. Data gathered at these touch points, once interpreted, provide information that affects touch points inside the company. For example, interpreted information may be redirected to marketing research, to develop profiles of extended warranty purchasers; to production, to analyze recurring problems and repair components; and to accounting, to establish cost-control models for repair service calls. With a CRM system, touch points become critical parts of the service delivery process.

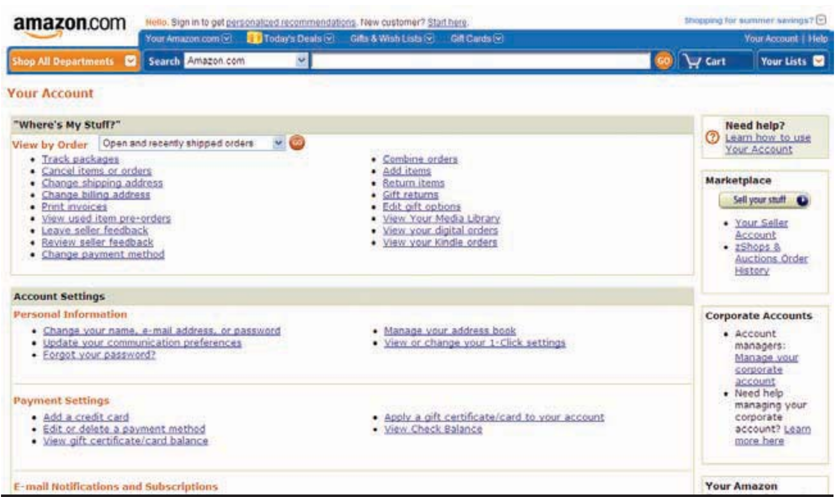


PHOTO © T/K

When users log on to the Amazon.com as either members or guests, their queries and purchases are recorded and tracked. From that initial touch point, every time users enter the site, their preferences are shown first.

Web-based interactions are an increasingly popular touch point for customers to communicate with companies on their own terms. Instead of wasting time with phone numbers and mail surveys, companies are publicizing their Web sites as the first touch point for customer interactions. Web users can evaluate and purchase products, make reservations, input preferential data, and provide customer feedback on services and products. Data from these Web-based interactions are then captured, compiled, and used to segment customers, refine marketing efforts, develop new products, and deliver a degree of individual customization to improve customer relationships.

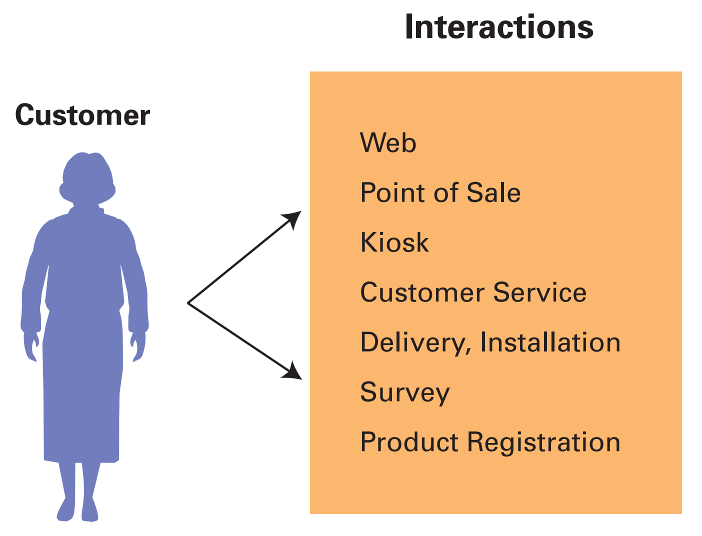
point-of-sale interactions Communications between customers and organizations that occur at the point of sale, normally in a store.

When users log on to the Amazon Books and Music Web site), for example, as either members or guests, their queries and purchases are recorded and tracked. From that initial touch point, every time users enter the site, their preferences are shown first. If they have purchased any books or music in the past, the site will recommend new books or CDs from either the same or a similar author or artist. Similarly, if customers request a book by a particular author without making a purchase, they will be informed on a subsequent visit about new material that author has for sale.[10]

Another touch point is through **point-of-sale interactions** in stores or at information kiosks. Many point-of-sale software packages enable customers to easily provide information about themselves without feeling that their privacy has been violated. The information is then used in two ways: for marketing and merchandising activities, and to accurately identify the store's best customers and the types of products they buy. Data collected at point-of-sale interactions is also used to increase customer satisfaction through the development of in-store services and customer recognition promotions. For example, Borders and Waldenbooks have joined together to offer a Platinum Visa Card that allows members to collect points for making purchases and redeem them for an in-store gift certificate. The companies can then track purchases and identify the best customers.

REVIEW LEARNING OUTCOME

LO 3 Understand interactions with the current customer base

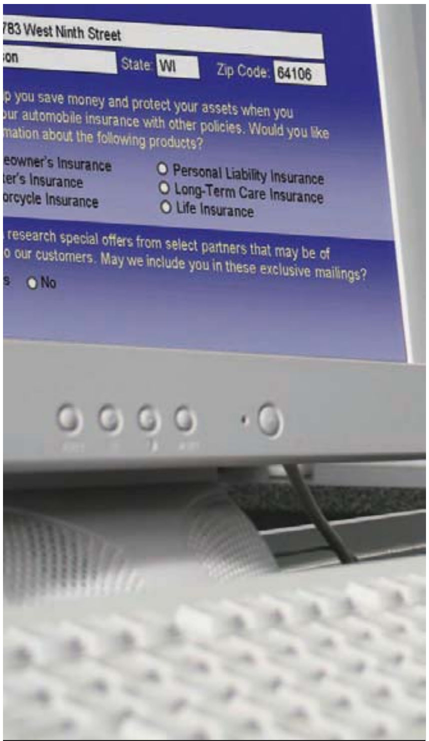


LO 4
Capture Customer Data

Vast amounts of data can be obtained from the interactions between an organization and its customers. Therefore, in a CRM system, the issue is not how much data can be obtained, but rather what types of data should be acquired and how the data can effectively be used for relationship enhancement.

The traditional approach for acquiring data from customers is through channel interactions. Channel interactions include store visits, conversations with salespeople, interactions via the Web, traditional phone conversations, and wireless communications, such as cell phone conversations and satellite communications. In a CRM system, channel interactions are viewed as prime information sources based on the channel selected to initiate the interaction rather than on the data acquired. For example, if a consumer logs on to the Sony Web site to find out why a Sony device is not functioning properly and the answer is not available online, the consumer is then referred to a page where he or she can describe the problem. The Web site then e-mails the problem description to a company representative, who will research the problem and reply via e-mail. Furthermore, Sony will follow up with a brief satisfaction survey also sent via e-mail. Sony continues to use the e-mail mode of communication because the customer has established this as the preferred method of contact.[11]

Interactions between the company and the customer facilitate collection of large amounts of data. Companies can obtain not only simple contact information (name, address, phone number), but also data pertaining to the customer's current relationship with the organization—past purchase history, quantity and frequency



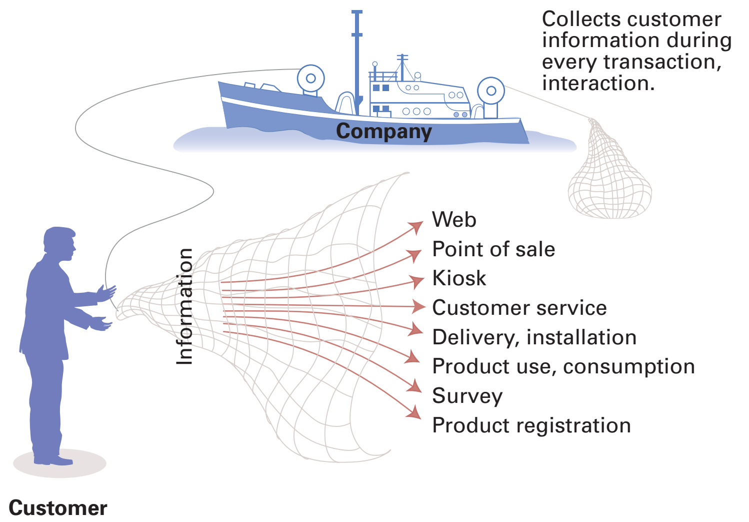
GEICO routinely collects customer data during policy renewals so that it can plan new products and market new services towards its current customers. An important touch point for GEICO is its Web site.

of purchases, average amount spent on purchases, sensitivity to promotional activities, and so forth. GEICO Insurance Company, for example, at the time of policy renewal for its auto insurance customers, requests information pertaining to lifestyles (activities, interests, opinions, etc.), cultural factors (ethnicity, religion, etc.), and customer life stage (family composition, number and age of children, children living at home, etc.) for the purposes of pricing and customizing insurance packages for its customers. These data are also used for planning new product offerings such as vehicle maintenance insurance and gap insurance for lease customers along with cross-selling other GEICO services such as life insurance, home insurance, and marine insurance.[12]

In this manner, a lot of information can be captured from one individual customer across several touch points. Multiply this by the thousands of customers across all of the touch points with an organization, and the volume of data can rapidly become unmanageable for company personnel. The large volumes of data resulting from a CRM initiative can be managed effectively only through the use of technology. Furthermore, once customer data are collected, the question of who owns those data becomes extremely salient.

REVIEW LEARNING OUTCOME

LO4 Outline the process of capturing customer data



LO5
Store and Integrate Customer Data

Customer data are only as valuable as the system in which the data are stored and the consistency and accuracy of the data captured. Gathering data is further complicated by the fact that data needed by one unit of the organization, such as sales and marketing, often are generated by another area of the business or even a third-party supplier, such as an independent marketing research firm. Thus, companies must use information technology to capture, store, and integrate strategically important customer information. This process of centralizing data in a CRM system is referred to as data warehousing.

A data warehouse is a central repository (*database*) of customer data collected by an organization. Essentially, it is a large computerized file of all information

data warehouse
A central repository for data from various functional areas of the organization that are stored and inventoried on a centralized computer system so that the information can be shared across all functional departments of the business.

database
A collection of data, especially one that can be accessed and manipulated by computer software.

response list
A customer list that includes the names and addresses of individuals who have responded to an offer of some kind, such as by mail, telephone, direct-response television, product rebates, contests or sweepstakes, or billing inserts.

compiled list
A customer list that is developed by gathering names and addresses from telephone directories and membership rosters, usually enhanced with information from public records, such as census data, auto registrations, birth announcements, business start-ups, or bankruptcies.

collected in the previous phase of the CRM process, for example, information collected in channel, transaction, and product/service touch points. The core of the data warehouse is the database, "a collection of data, especially one that can be accessed and manipulated by computer software."[13] The CRM database focuses on collecting vital statistics on consumers, their purchasing habits, transaction methods, and product usage in a centralized repository that is accessible by all functional areas of a company. Traditionally, this information was stored in separate computer systems throughout the company. By utilizing a data warehouse, however, marketing managers can quickly access vast amounts of information required to make decisions. For example, Continental Airlines used to store data in a variety of operational systems that could not be integrated. As a result, managers did not have the depth and breadth of information to facilitate their decision-making capabilities. Now the Continental data warehouse centralizes data from 41 sources. The warehouse is accessible by 35 departments and 1,300 employees. The database content includes everything from flight schedules, seat inventory, and customer profiles to employee and crew payroll. Even aircraft parts and maintenance are being added to the system to aid in distribution decision making.[14]

When a company builds its database, the first step is to develop a list. Usually, this is in the form of a response list, based on customers who have indicated interest in a product or service, or a compiled list, created by an outside company that has collected names and contact information for potential consumers. Response lists tend to be especially valuable because past behavior is a strong predictor of future behavior and because consumers who have indicated interest in the product or service are more prone to purchase. Compiled lists usually are prepared by an outside company and are available for purchase. A compiled list generally includes names and addresses gleaned from telephone directories or membership rosters. Many lists are available, ranging from those owned by large list companies, such as Dun & Bradstreet for business-to-business data and Donnelley and R. L. Polk for consumer lists, to small groups or associations that are willing to sell their membership lists. Data compiled by large data-gathering companies usually are very accurate.

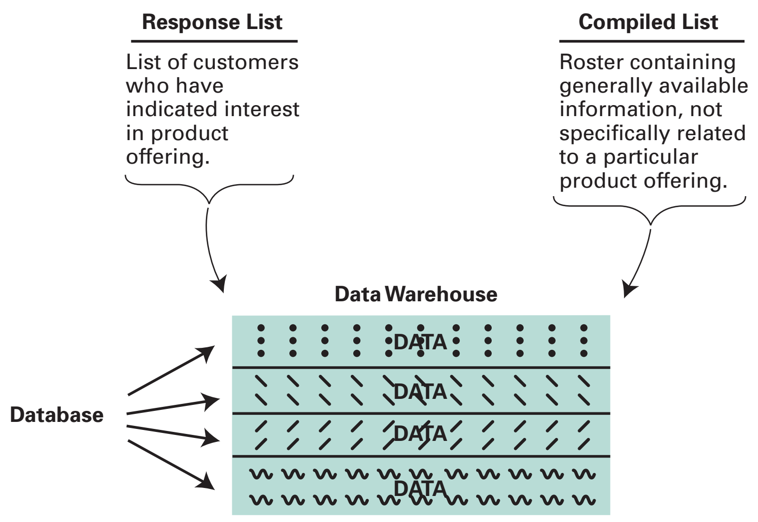
In this phase companies are usually collecting channel, transaction, and product/service information such as store, salesperson, communication channel, contact information, relationship, and brands. For example, when Philips wanted to determine how to best sell its CoolSkin Shaver accessories, it used existing information to expand its database. By sending an e-mail to registered users, Philips was able to collect information including whether consumers purchased online; if so, the "landing page" on the Web site; the number of "unsubscribes" when sent an e-mail; and the timeliness of response.[15]

A customer database becomes even more useful to marketing managers when it is enhanced to include more than simply a customer's or prospect's name, address, telephone number, and transaction history. Database enhancement involves purchasing information on customers or prospects to better describe their needs or determine how responsive they might be to marketing programs. Types of enhancement data typically include demographic, lifestyle, or behavioral information. Lands' End, for example, has enhanced its database to better understand purchasing patterns. The database not only pinpoints popular clothing items, but also attempts to explain why. In one instance, sales of raincoats increased sharply in the Northeast. Because the database is linked to regional weather information, analysts were able to explain the sudden boost in raincoat sales.[16]

Database enhancement can increase the effectiveness of marketing programs. By learning more about their best and most profitable customers, marketers can maximize the effectiveness of marketing communications and cross-selling. Database enhancement also helps a company find new prospects. Before opening a new store, H-E-B Grocery Company (**http://www.heb.com**) uses database enhancement and customer profiling to identify and learn as much as possible about potential customers. Each store is then designed to be unique and to offer the products those customers want. When the company opened one of its upscale Central Market stores in Fort Worth, Texas, customer profiles indicated that Fort Worth residents have a strong sense of Western heritage. The Fort Worth location, therefore, offers customers chipotle-smoked barbecue ribs, game birds, and briskets. The store has also adjusted the way it cuts and sells beef to meet local preferences, and it carries an expanded selection of peppers and fresh tortillas for its Hispanic customers. Once open, the stores continue to use databases to collect information about customer preferences and to tweak product offerings.

REVIEW LEARNING OUTCOME

LO 5 Describe the use of technology to store and integrate customer data



Multinational companies building worldwide databases often face difficult problems when pulling together internal data about their customers. Differences in language, computer systems, and data-collection methods can be huge obstacles to overcome. In spite of the challenges, many global companies are committed to building databases. Unilever is using the Internet not only to educate consumers about the brand but also to develop relationships with its customers by providing helpful information. Web site visitors can get information on removing stubborn stains and solving similar consumer problems. They also receive a discount on their next purchase in exchange for completing an online questionnaire. With diligent effort, Unilever has collected information on more than 30 million loyal customers from numerous countries.[17]

LO 6 Identifying the Best Customers

CRM manages interactions between a company and its customers. To be successful, companies must identify customers who yield high profits or potential profits. To do so, significant amounts of data must be gathered from customers, stored and integrated in the data warehouse, and then analyzed and interpreted for common patterns that can identify homogeneous customers who are different from other customer segments. Because not all customers are the same, organizations need to develop interactions that target *individual* customer needs and wants. Likewise, not all customers do generate the same revenue for a company. Recall, from Chapter 8, the 80/20 principle—80 percent of a company's revenue is generated by 20 percent of its customers. Therefore, the question becomes, how do we identify the 20 percent of our customer base that contributes 80 percent of our revenue? In a CRM system, the answer is data mining.

DATA MINING

Data mining is used to find hidden patterns and relationships in the customer data stored in the data warehouse. It is a data analysis approach that identifies patterns of characteristics that relate to particular customers or customer groups. Although businesses have been conducting such analyses for many years, the procedures typically were performed on small data sets containing as few as 300 to 400 customers. Today, companies analyze billions of customer shopping patterns stored in their data warehouses. Nokia, for example, examined over 6 billion pieces of data to develop its

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Data mining is used in a wide range of companies—large supermarket chains, music stores, and even casinos, such as Harrah's Entertainment.

N-Series mobile phone. Wal-Mart's data warehouse, believed to be second in size only to the Pentagon's, contains over 4,000 terabytes (trillions of characters) of customer and market data. Wal-Mart uses its huge data warehouse to help each of its stores adapt its merchandising mix to local neighborhood preferences.

Using data mining, marketers can search the data warehouse, capture relevant data, categorize significant characteristics, and develop customer profiles. For example, in the Philips razor example, marketers were attempting to build a relationship with consumers through e-mail. By assessing response and nonresponse rates along with online purchases, they developed a profile of consumers likely to purchase CoolSkin accessories over the Internet. Moreover, once Philips was successful with CoolSkin accessories, it used this approach on other product lines.[18]

When using data mining, it is important to remember that the real value is in the company's ability to transform its data from operational bits and bytes into information marketers need for successful marketing strategies. Companies must go beyond merely creating a mailing list. They must analyze the data to identify and profile the best customers, calculate their lifetime value, and ultimately predict purchasing behavior through statistical modeling.

A wide range of companies have used data mining successfully. Albertson's Supermarkets use data mining to identify commonly purchased items that should be placed together on shelves and to learn what soft drinks sell best in different parts of the country. Using data mining, Camelot Music discovered that a large number of senior citizens were purchasing rap and alternative music. When managers investigated further, they discovered seniors were buying the music as gifts for their grandchildren. Finally, TheKnot.com, a Web site that helps plan weddings, asks users to register and provide basic information. Its database stores information and creates an initial profile of a customer. From the initial contact, the Web site gathers data as the customer uses the site. For example, when a user adds a product to the registry, the database is updated to reflect that change. Thus, if a consumer adds a different brand or product to the list, the site will tailor product recommendations to reflect that change.[19]

Before the information is leveraged, several types of analyses are often run on the data. These analyses include customer segmentation, recency-frequency-monetary analysis (RFM), lifetime value analysis (LTV), and predictive modeling.

Customer Segmentation

Recall that *customer segmentation* is the process of breaking large groups of customers into smaller, more homogeneous groups. This type of analysis generates a "profile" or picture of the customers' similar demographic, geographic, and psychographic traits as well as their previous purchase behavior; it focuses particularly on the best customers. Profiles of the best customers can be compared and contrasted with other customer segments. For example, a bank could segment consumers on frequency of usage, credit, age, and turnover. Once a profile of the best customer is developed using these criteria, it can be used to screen other potential consumers. Similarly, customer profiles can be used to introduce customers selectively to specific marketing actions. For example, young customers with an open mind can be introduced to home banking, and older, well- established customers to investment opportunities. See Chapter 8 for a detailed discussion of segmentation.

Recency-Frequency-Monetary Analysis (RFM)

Customers who have purchased recently and often and have spent considerable money are more likely to purchase again. Recency-frequency-monetary analysis (RFM) identifies those customers most likely to purchase again because they have bought recently, bought frequently, or spent a specified amount of money with the firm. Firms develop equations to identify the "best customers" (often the top

lifetime value analysis (LTV) A data manipulation technique that projects the future value of the customer over a period of years using the assumption that marketing to repeat customers is more profitable than marketing to first-time buyers.

predictive modeling A data manipulation technique in which marketers try to determine, based on some past set of occurrences, what the odds are that some other occurrence, such as a response or purchase, will take place in the future.

20 percent of the customer base) by assigning a score to customer records in the database on how often, how recently, and how much they have spent. Customers are then ranked to determine which ones move to the top of the list and which ones fall to the bottom. The ranking provides the basis for maximizing profits because it enables the firm to use the information in its customer database to select those persons who have proved to be good sources of revenue. Casino operator Harrah's Entertainment used data mining and RFM to identify 90 market segments that it can target with its marketing programs. Using direct feedback from the slots as to whether its strategies are working, Harrah's continuously tweaks its marketing tactics to focus on the most profitable segments.[20]

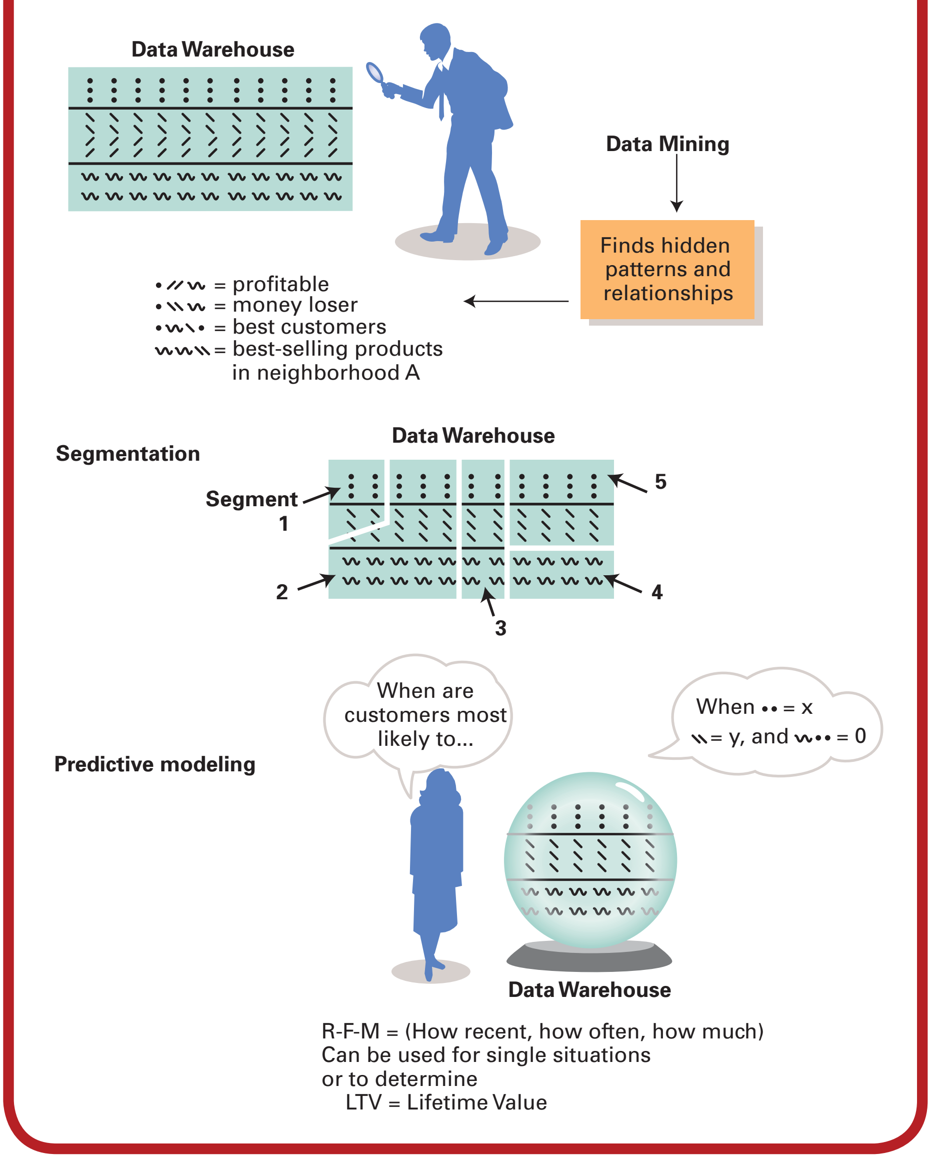
Lifetime Value Analysis (LTV)

Recency, frequency, and monetary data can also be used to create a lifetime value model on customers in the database. Whereas RFM looks at how valuable a customer currently is to a company, lifetime value analysis (LTV) projects the future value of the customer over a period of years. One of the basic assumptions in any lifetime value calculation is that marketing to repeat customers is more profitable than marketing to first-time buyers. That is, it costs more to find a new customer in terms of promotion and gaining trust than to sell more to a customer who is already loyal.

Customer lifetime value has a number of benefits. It shows marketers how much they can spend to *acquire* new customers, it tells them the level of spending to *retain* customers, and it facilitates targeting new customers who look as though they will be profitable customers. Cadillac has calculated the lifetime value of its top customers at $332,000. Similarly, Pizza Hut figures its best customers are worth $8,000 in bottom-line lifetime value.

REVIEW LEARNING OUTCOME

LO6 Describe how to identify the best customers



Predictive Modeling

The ability to reasonably predict future customer behavior gives marketers a significant competitive advantage. Through predictive modeling, marketers try to determine, based on some past set of occurrences, what the odds are that some other occurrence, such as an Internet inquiry or purchase, will take place in the future. SPSS Predictive Marketing is one tool marketers can use to answer questions about their consumers. The software requires minimal knowledge

campaign management Developing product or service offerings customized for the appropriate customer segment and then pricing and communicating these offerings for the purpose of enhancing customer relationships

of statistical analysis. Users operate from a prebuilt model, which generates profiles in three to four days. SPSS also has an online product that predicts Web site users' behavior. Harrah's Entertainment, Inc. uses predictive modeling to attract millions of customers. Its models include the ages, gender, zip codes, amount of time spent gambling, and how much individuals have won or lost. Analyses of the data enable Harrah's to target individuals with special offers, like getaway weekends and gourmet restaurant meals, to attract them back to the casinos to gamble more. Predictive modeling has enabled Harrah's to average 22 percent growth for the past five years while its stock price has tripled.[21] Harrah's management uses predictive modeling to develop long-term, personalized, and profitable relationships with each of their customers.

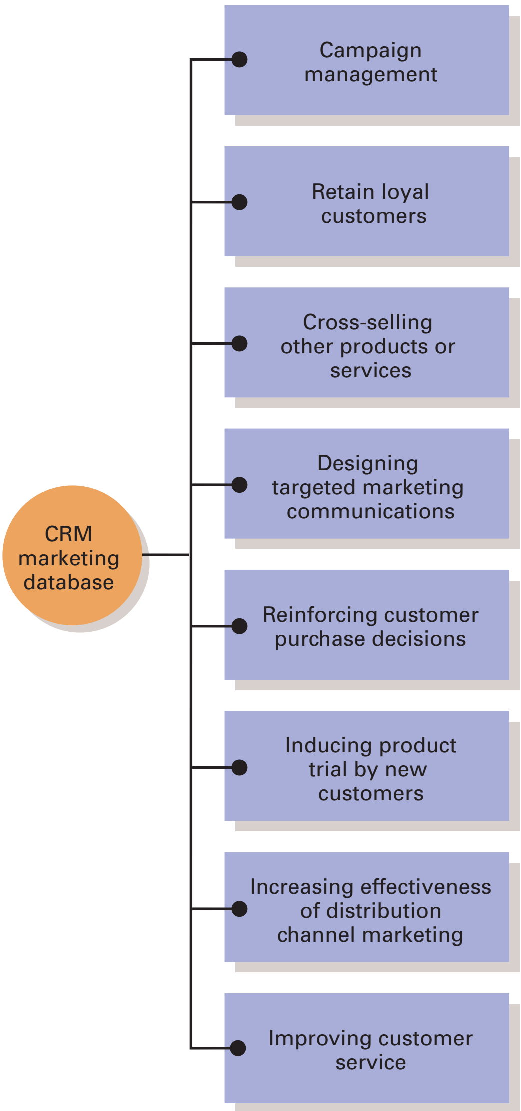
LO7

Leverage Customer Information

Data mining identifies the most profitable customers and prospects. Managers can then design tailored marketing strategies to best appeal to the identified segments. In CRM this is commonly referred to as leveraging customer information to facilitate enhanced relationships with customers. Exhibit 21.3 shows some common CRM marketing database applications.

Exhibit 21.3

Common CRM Marketing Database Applications



CAMPAIGN MANAGEMENT

Through campaign management, all areas of the company participate in the development of programs targeted to customers. Campaign management involves monitoring and leveraging customer interactions to sell a company's products and to increase customer service. Campaigns are based directly on data obtained from customers through various interactions. Campaign management includes monitoring the success of the communications based on customer reactions through sales, orders, callbacks to the company, and the like. If a campaign appears unsuccessful, it is evaluated and changed to better achieve the company's desired objective. Stave Puzzles, the "Rolls-Royce" of puzzles, produces handcrafted wood puzzles. Each puzzle is unique and can be customized as the customer desires. Steve Richardson, the company's cofounder, has narrowed his customer base to his "Hot Hundred" most valuable customers. To manage his customer base and ensure they are receiving optimal service, he tracks not only standard information, such as contact data and orders, but also birthdays, anniversaries, relationships between customers, phone conversations, inquiries, and workshop visits.[22]

Campaign management involves developing customized product and service offerings for the appropriate customer segment, pricing these offerings attractively, and communicating these offers in a manner that enhances customer relationships. Customizing product and service offerings requires managing multiple interactions with customers, as well as giving priority to those products and services that are viewed as most desirable for a specifically designated customer. Even within a highly defined market segment, individual customer differences will emerge. Therefore, interactions among customers must focus on individual experiences, expectations, and desires. Stave Puzzles customizes its marketing campaigns by tailoring mailouts to eight different segments. For example, the monthly buyers and top 10 percent of the customers receive individual reminder notes about special occasions and previous purchases.

RETAINING LOYAL CUSTOMERS

If a company has identified its best customers, then it should make every effort to maintain and increase their loyalty. When a company retains an additional 5 percent of its customers each year, profits will increase by as much as 25 percent. What's more, improving customer retention by a mere 2 percent can decrease costs by as much as 10 percent.[23] For example, The Palace of Auburn Hills, a sporting venue, is home to the NBA Detroit Pistons and the WNBA Detroit Shock. To increase game attendance, the arena developed its MyPal rewards card, which enables fans to receive e-mail updates. As a result, game attendance has increased for all types of consumers.[24]

Loyalty programs reward loyal customers for making multiple purchases. The objective is to build long-term mutually beneficial relationships between a company and its key customers. Marriot, Hilton, and Starwood Hotels, for instance, reward their best customers with special perks not available to customers who stay less frequently. Travelers who spend a specified number of nights per year receive reservation guarantees, upgrades to better rooms, welcome gifts like fruit baskets and wine in their rooms, free phone service, and access to concierge lounges. In addition to rewarding good customers, loyalty programs provide businesses with a wealth of information about their customers and shopping trends that can be used to make future business decisions. CVS, the U.S. drugstore chain with the most stores, has an ExtraCare program that allows customers to register for a card that is swiped prior to each purchase and gives discounts and offers special in-store promotions. The coupons and discounts are based on purchase history, which enables the company to sell more products. The ExtraCare program helps CVS respond to what customers really want, based on information collected from card sales, and has attracted more than 50 million customers.[25]

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CROSS-SELLING OTHER PRODUCTS AND SERVICES

CRM provides many opportunities to cross-sell related products. Marketers can use the database to match product profiles and consumer profiles so that they can cross-sell customers products that match their demographic, lifestyle, or behavioral characteristics. American Collegiate Marketing, a magazine subscription service targeted to students and educators (**http://www.magazineline.com**), uses past customer purchase information gleaned from its database of millions of magazine subscribers to feature new magazines that may interest the customer. Past purchase behavior may show that subscribers to *Sports Illustrated,* for instance, are also interested in general news magazines such as *Time* and *Newsweek*. Similarly, to increase purchasing across different departments and in different product lines, Wegmans Food Markets monitors sales using a frequent buyer card. Using data mining, it discovered that 80 percent of shoppers buying baby food also bought flowers. As a result, Wegmans was able to develop a more effective method for cross-selling products.[26]

Internet companies use product and customer profiling to reveal cross-selling opportunities while a customer is surfing their site. Past purchases on a particular Web site and the site a surfer comes from give online marketers clues about the surfer's interests and what items to cross-sell. Fry's Outpost electronics (**http://www.outpost.com**), a computer-goods e-tailer, adjusts the pages visitors see depending on what they click on at the site or what they purchased in the past. For instance, if a surfer always goes to computer game pages or has purchased games in the past, Outpost will automatically place offers for other game titles on part of the screen. Depending on what a shopper puts in a shopping cart, Outpost will flash promotions

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for related items—a leather case for someone who is buying a PDA, for example.

DESIGNING TARGETED MARKETING COMMUNICATIONS

Using transaction and purchase data, a database allows marketers to track customers' relationships to the company's products and services and modify the marketing message accordingly. For example, Kraft Foods teamed with Wegmans Food Markets to determine which advertising campaigns were most effective for frequent buyers of Kraft Macaroni & Cheese. Kraft used the results to better reach its frequent buyers in future campaigns.[27]

Customers can also be segmented into infrequent users, moderate users, and heavy users. A segmented communications strategy can then be developed based on which group the customer falls into. Communications to infrequent users might encourage repeat purchases through a direct incentive such as a limited-time price discount for ordering again. Communications to moderate users may use fewer incentives and more reinforcement of past purchase decisions. Communications to heavy users would be designed around loyalty and reinforcement of the purchase rather than price promotions. For example, Nike Store Toronto offers the Air Max Club (AMC), a loyalty club for customers. Club members can collect points and redeem them for gift certificates, movies, and books. Customers considered "most valuable" are identified when they swipe their card to collect points, thereby alerting the salesperson. A message on the salesperson's screen indicates that the customer should receive a special thank-you and possibly a prize. The system also generates customized coupons based on purchase history. The company has found that club members spend about 50 percent more than the average customer.[28]

REINFORCING CUSTOMER PURCHASE DECISIONS

As you learned in the consumer behavior chapter, cognitive dissonance is the feeling consumers experience when they recognize an inconsistency between their values and opinions and their purchase behavior. In other words, they doubt the soundness of their purchase decision and often feel anxious. CRM offers marketers an excellent opportunity to reach out to customers to reinforce the purchase decision. By thanking customers for their purchases and telling them they are important, marketers can help cement a long-term, profitable relationship. Guests staying at the quaint Village Country Inn nestled in the Green Mountains of Vermont receive a handwritten thank-you note from the inn's proprietors within a week of their stay. The note thanks the guests for visiting and encourages them to return in the future.

Updating customers periodically about the status of their order reinforces purchase decisions. Postsale e-mails also afford the chance to provide more customer service or cross-sell other products. Minutes after customers order merchandise from Amazon.com's Web site, for example, they receive an e-mail acknowledging their order. Every few days thereafter, customers receive updates that allow them to track the shipment of the order, from ship date to receipt. Similarly, Sumerset Houseboats builds customized, luxury houseboats priced at about $250,000 each. The company uses its Web site to monitor customer profiles, post company information, and communicate with customers. For example, it posts daily pictures of progress on houseboats being built. By reinforcing customers' decisions, Sumerset is able to offset the feeling of cognitive dissonance.[29]

INDUCING PRODUCT TRIAL BY NEW CUSTOMERS

Although significant time and money are expended on encouraging repeat purchases by the best customers, a marketing database is also used to identify new customers. Because a firm using a marketing database already has a profile of its best customers, it can easily use the results of modeling to profile potential customers. EATEL, a regional telecommunications firm, uses modeling to identify prospective residential and commercial telephone customers and successfully attract their business.

Marketing managers generally use demographic and behavioral data overlaid on existing customer data to develop a detailed customer profile that is a powerful tool for evaluating lists of prospects. For instance, if a firm's best customers are 35 to 50 years of age, live in suburban areas, own luxury cars, like to eat at Thai restaurants, and enjoy mountain climbing, then the company can find prospects already in its database or customers who currently are identified as using a competitor's product that match this profile. Procter & Gamble uses its Web site to test customer interest in new products. Customers who visit the Web site are encouraged to sign up for free trial samples and then provide feedback. P&G also uses the demographic data and customer feedback to make product and promotion decisions.

INCREASING EFFECTIVENESS OF DISTRIBUTION CHANNEL MARKETING

In Chapter 13 you learned that a marketing channel is a business structure of interdependent organizations, such as wholesalers and retailers, that move a product from the producer to the ultimate consumer. Most marketers rely on indirect channels to move their products to the end user. Thus, marketers often lose touch with the customer as an individual since the relationship is really between the retailer and the consumer. Marketers in this predicament often view their customers as aggregate statistics because specific customer information is difficult to gather.

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American ExpressPay keys contain a radio-frequency identification chip that enables cardholders to make instant purchases at places like Carl's Jr. restaurants. The ExpressPay keys are contactless versions of American Express credit cards, requiring the user to simply tap the card on a special reader to make a purchase.

With CRM databases, manufacturers now have a tool to gain insight into who is buying their products. Instead of simply unloading products into the distribution channel and leaving marketing and relationship building to dealers, auto manufacturers today are using Web sites to keep in touch with customers and prospects, learn about their lifestyles and hobbies, understand their vehicle needs, and develop relationships in hopes that these consumers will reward them with brand loyalty in the future. BMW and Mercedes-Benz USA, as well as other vehicle manufacturers, have databases with names of millions of consumers who have expressed an interest.

With many brick-and-mortar stores setting up shop online, companies are now challenged to monitor purchases of customers who shop both in-store and online. This concept is referred to as multichannel marketing. After Lands' End determined that multichannel customers are the most valuable, the company targeted marketing campaigns toward retaining these customers and increased sales significantly. Talbot's and Victoria's Secret have also developed successful campaigns to serve multichannel customers.

Companies are also using radio-frequency identification (RFID) technology to improve distribution. The technology uses a microchip with an antenna that tracks anything from a soda can to a car. A computer can locate the product anywhere. The main implication of this technology is that companies will enjoy a reduction in theft and loss of merchandise shipments and will always know where merchandise is in the distribution channel. Moreover, as this technology is further developed, marketers will be able to gather essential information related to product usage and consumption.[30]

IMPROVING CUSTOMER SERVICE

CRM marketing techniques increasingly are being used to improve customer service. The level of customer service provided by companies is influential in customer retention. *Customer retention* is the percentage of customers that repeatedly purchase products from a company. Boise Cascade Office Products uses CRM to compete against competitors like Staples and Office Depot. The company recently changed its culture to become more customer-centric. Sales reps are sent out to meet one-to-one with customers, and when customers place orders, either by phone or the Internet, information technology software automatically accesses their transaction history and customizes the response.

PRIVACY CONCERNS AND CRM

Before rushing out to invest in a CRM system and build a database, marketers should consider consumers' reactions to the growing use of databases. Many Americans and customers abroad are concerned about databases because of the potential for invasion of privacy. The sheer volume of information that is aggregated in databases makes this information vulnerable to unauthorized access and use. A fundamental aspect of marketing using CRM databases is providing valuable services to customers based on knowledge of what customers really value. It is critical, however, that marketers remember that these relationships should be built on trust. Although database technology enables marketers to compile

ETHICS in Marketing

Privacy Issues Must Be Resolved for CRM's Success

CRM is a hot marketing topic and a popular business tool. But it also sparks hot debates regarding consumers' privacy. American businesses have collected consumer data for years. Policies and laws govern what businesses can do with that information once it is collected. Current laws cover several industries including finance, health care, retail, automotive and transportation, technology, and direct marketing. The Gramm-Leach-Bliley Act enforces privacy guidelines for financial information, the Health Insurance Portability and Accountability Act (HIPAA) regulates medical records, and the National Do-Not-Call list governs telemarketing. Most recently, the CAN-SPAM Act provided guidelines for e-mail.

Companies have taken initiatives, too. Many have developed independent privacy policies designed to govern how they collect, use, share, and protect the personal information of consumers and employees. According to the 2003 Benchmark Study of Corporate Privacy Practices Report, 98 percent of U.S. companies have a privacy policy in effect. Nevertheless, more than half of those companies feel their policy may be difficult to understand. One problem is that only 53 percent require mandatory training for policy enforcement. Consequently, consumer information is still vulnerable to unethical corporate practices.

Despite consumers' concerns, company executives realize that consumer information is very profitable. Companies can profit by sharing the information with a third party or by purchasing third-party information to build a more comprehensive database. As a result, companies are struggling to balance consumer trust and profitability. For example, the Walt Disney Company used to have a strict policy that did not allow it to share information collected on its Web site with third parties. Once executives realized the value of the information, however, they amended the privacy policy to enable third-party companies to send promotions to consumers. To ensure continued consumer trust, Disney allows consumers to opt in or opt out of third-party promotions. Additionally, Disney offers consumers updated privacy information on its Web site and sends e-mails to registered users explaining any privacy policy changes.[31]

How does a firm's privacy policy affect your purchasing decisions? Do you think it is ethical for a company to post a privacy policy but not have mandatory enforcement? What are the most important issues in establishing a privacy policy for a business?

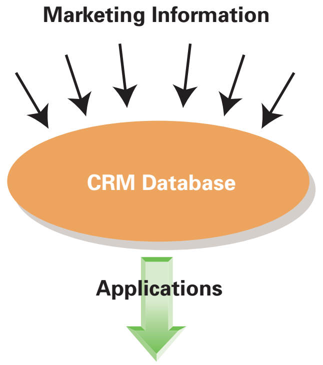
ever-richer information about their customers that can be used to build and manage relationships, if these customers feel their privacy is being violated, then the relationship becomes a liability.

The popularity of the Internet for e-commerce and customer data collection and as a repository for sensitive customer data has alarmed privacy-minded customers. Online users complain loudly about being "spammed," and Web surfers, including children, are routinely asked to divulge personal information to access certain screens or purchase goods or services. Internet users are disturbed by the amount of information businesses collect on them as they visit various sites in cyberspace. Indeed, many users are unaware of how personal information is collected, used, and distributed. The government actively sells huge amounts of personal information to list companies. State motor vehicle bureaus sell names and addresses of individuals who get driver's licenses. Hospitals sell the names of women who just gave birth on their premises. Consumer credit databases are often used by credit card marketers to prescreen targets for solicitations. Online and off-line privacy concerns are growing and ultimately will have to be dealt with by businesses and regulators.

Privacy policies for companies in the United States are largely voluntary, and regulations on how personal data are collected and used are being developed. But collecting data on consumers outside the United States is a different matter. For database marketers venturing beyond U.S. borders, success requires careful navigation of foreign privacy laws. For example, under the European Union's European Data Protection Directive, any business that trades with a European organization must comply with the EU's rules for handling information about individuals or risk prosecution. More than 50 nations have, or are developing, privacy legislation. Europe has the strictest legislation regarding the collection and use of customer data, and other countries are looking to that legislation when formulating their policies. The "Ethics in Marketing" box provides more perspectives on resolving CRM privacy issues.

REVIEW LEARNING OUTCOME

LO7 Explain the process of leveraging customer information throughout the organization



- ✓ Campaign management
- ✓ Retaining loyal customers
- ✓ Cross-selling other products and services
- ✓ Designing targeted marketing communications
- ✓ Reinforcing customer purchase decisions
- ✓ Inducing product trial by new customers
- ✓ Increasing effectiveness of distribution channel marketing
- ✓ Improving customer service

sources from which Continental Airlines centralizes data > **41**

35 < departments through which Continental makes data available

customers from whom Unilever has collected information > **30 million**

terabytes of data in Wal-Mart's warehouse > **4,000**

90 < market segments identified by the casino operator Harrah's

lifetime value of a top Cadillac customer > **$332,000**

$8,000 < lifetime value of a top Pizza Hut customer

segments receiving mailouts from Stave Puzzles > **8**

80 < percentage of baby-food buyers who also purchase flowers

price of a customized houseboat from Sumerset > **$250,000**

Review and Applications

LO 1

Define customer relationship management. Customer relationship management (CRM) is a company-wide business strategy designed to optimize profitability, revenue, and customer satisfaction by focusing on highly defined and precise customer groups. This is accomplished by organizing the company around customer segments, encouraging and tracking customer interaction with the company, fostering customer-satisfying behaviors, and linking all processes of a company from its customers through its suppliers.

1.1 Identify the six components of the CRM process.

TEAM

1.2 Form a team and identify several local businesses that would benefit from a CRM strategy. Select one business and outline a plan for implementing a CRM strategy for that business. You may want to visit the company and interview managers about their current initiatives. When you have completed your CRM plan, share it with the class—and the company.

WRITING

ONLINE

1.3 General Motors installs the "OnStar" system in many of its vehicles. OnStar is a location, information, and communication system available to drivers who wish to subscribe to the service. Go to the OnStar Web site, **http:// www.onstar.com**, and read about some of the services that are offered to consumers. Based on what you learn, write a short report describing the various ways that OnStar can be used as a CRM tool, specifically in the context of creating interactions, gathering customer data, and customizing service offerings to customers.

LO 2

Explain how to identify customer relationships with the organization. Companies that implement a CRM system adhere to a customer-centric focus or model. A customer-centric company focuses on learning the factors that build long-lasting relationships with valuable customers and then builds its system on what satisfies and retains those customers. Building relationships through CRM is a strategic process that focuses on learning, managing customer knowledge, and empowerment.

2.1 Briefly explain the concept of a customer-centric focus. Why is this so important in a CRM process?

2.2 What is meant by knowledge management? Why is it so important in a CRM system?

LO 3

Understand interactions with the current customer base. The interaction between the customer and the organization is considered to be the foundation on which a CRM system is built. Only through effective interactions can organizations learn about the expectations of their customers, generate and manage knowledge about them, negotiate mutually satisfying commitments, and build long-term relationships. Effective management of customer interactions recognizes that customers provide information to organizations across a wide variety of touch points. Consumer-centric organizations are implementing new and unique approaches for establishing interactions specifically for this purpose. They include Web-based interactions, point-of-sale interactions, and transaction-based interactions.

3.1 Develop a plan for establishing and managing interactions with a business's customers. In this plan, identify the key touch points for customers, explain how the data warehouse would be designed, and indicate the main interaction methods that would be promoted to the customer.

LO 4

Outline the process of capturing customer data. Based on the interaction between the organization and its customers, vast amounts of information can be obtained. In a CRM system, the issue is not how much data can be obtained, but rather what type of data should be acquired and how those data can be used effectively for relationship enhancement. The channel, transaction, and product or service consumed all constitute touch points between a customer and the organization. These touch points represent possible areas within a business where customer interactions can take place and, hence, the opportunity for acquiring data from the customer.

ONLINE

WRITING

4.1 Assume you are the manager for a Hard Rock Café. Your boss has asked you to evaluate how the company is using its Web site to gather customer data. Go to the Web site for the Hard Rock (**http://www.hardrock.com**) and provide a detailed critique on how the site is used for capturing customer data. Comment on the types of customer data the Web site is designed to capture, and explain how those data would benefit your local Hard Rock operation.

LO5

Describe the use of technology to store and integrate customer data. Customer data gathering is complicated because information needed by one unit of the organization (e.g., sales and marketing) is often generated by another area of the business or even a third-party supplier (e.g., an independent marketing research firm). Because of the lack of standard structure and interface, organizations rely on technology to capture, store, and integrate strategically important customer information. The process of centralizing data in a CRM system is referred to as data warehousing. A data warehouse is a central repository of customer information collected by an organization.

5.1 Briefly explain the concept of a data warehouse. In the context of a CRM framework, why is a data warehouse such an important tool?

WRITING

5.2 What is being written about customer data in today's periodicals? Search your favorite database of articles using keywords like "customer data" and "data warehousing." Are certain industries better represented in the citation list generated by your search? Are certain issues more prevalent? Read a selection of at least three to four articles, and write a brief analysis of what is being discussed in the press regarding these CRM topics.

LO6

Describe how to identify the best customers. Customer relationship management, as a process strategy, attempts to manage the interactions between a company and its customers. To be successful, organizations must identify customers who yield high profitability or high potential profitability. To accomplish this task, significant amounts of information must be gathered from customers, stored and integrated in the data warehouse, and then analyzed for commonalities that can produce segments that are highly similar, yet different from other customer segments. A useful approach to identifying the best customers is recency-frequency-monetary (RFM) analysis. Data mining uses RFM, predictive modeling, and other approaches to identify significant relationships among several customer dimensions within vast data warehouses. These significant relationships enable marketers to better define the most profitable customers and prospects.

6.1 Explain the concept of data mining. Provide five examples of companies that are currently using data mining and explain why each is using it.

LO7

Explain the process of leveraging customer information throughout the organization. One of the benefits of a CRM system is the capacity to share information throughout the organization. This allows an organization to interact with all functional areas to develop programs targeted to its customers. This process is commonly referred to as campaign management. Campaign management involves developing customized product/service offerings for the appropriate customer segment and pricing and communicating these offerings for the purpose of enhancing customer relationships.

7.1 Campaign management is a benefit derived by an organization's ability to leverage and disseminate information throughout the company. Briefly define campaign management and explain how a business may apply it to its daily operations. In your answer, select a particular business as an example of effective campaign management.

ONLINE

7.2 What kind of product testing is currently going on at the Procter & Gamble Web site (**http://www.pg.com**)? Sign up to participate and find out how the company implements its one-to-one marketing plan through its Web site.

Key Terms

campaign management	644
compiled list	640
customer-centric	635
customer relationship management (CRM)	632
database	640
data warehouse	639
empowerment	635
interaction	636
knowledge management	635
learning	635
lifetime value analysis (LTV)	643
point-of-sale interactions	638
predictive modeling	643
response list	640
touch points	637

Exercises

APPLICATION EXERCISE

Understanding how companies use consumer information can be difficult if you have never had a job or internship that required you to use databases or customer profiles.[32]

Activity

1. Save all the direct-mail advertising that comes to your mailbox for at least a week. You may ask your parents or friends to collect direct mail that they receive as well.
2. Once you have your stack of mail, organize it according to the household that received it. For example, if friends and family helped you collect mail, then keep mail sent to each address together. Make a list of all material in each group.
3. To what kind of customer is each piece of mail targeted? What makes you think as you do?
4. Based on the content of the mail pieces, determine what kind of information the various companies have about you, your friends, or your family in their databases. Are there indications on the mailers about what kind of interactions the recipient has had with the sender of the marketing piece?
5. Write out an aggregate profile for each address. If you were a direct marketer, what kind of products and services would you market to each? What kind of offers would you create?

ETHICS EXERCISE

By combining several of its databases of parental purchasing behavior and the results of its market research, Maxwell, Inc., believes it has the tools to launch one-to-one marketing messages for the six- to nine-year-old fans of its JoyMax educational toy products without violating the law. In spite of potential parental backlash, Maxwell believes the approach will help it customize new children's products and increase the company's share of these profitable young customers.

Questions

1. What do you think? Should Maxwell use one-to-one marketing tools to communicate with children?
2. Does the AMA Statement of Ethics address marketing to children? Go to **http://www.marketingpower.com** and review the statement. Then, write a brief paragraph on how the AMA Statement of Ethics relates to Maxwell's dilemma.

Case Study: Petco.com

COURTESY, PETCO, INC.

TURNING NEGATIVE REVIEWS INTO POSITIVE SALES

On Petco.com you can buy a soft-sided travel carrier for your cat for only $19.99. You might think twice, though, after seeing that customers gave it only two "paws" out of five overall for pet satisfaction, appearance, and quality. The reviews reveal more serious reasons to hesitate before adding the product to your cart. A customer with the screen name "Disgruntled Bunny" reports: "The mesh on the sides was such poor quality that my cat was able to rip it to shreds and escape in a matter of seconds!" Another customer recommends buying a carrier with stronger sides, adding, "It costs more but is safer for your pet, so it's worth it."

Products have long been rated on sites like Amazon.com and those that exist entirely for customer reviews, but Petco was one of the first mainstream retailers to create a forum on its own Web site for criticism. The risk was obvious: customers could pan products and send buyers running. But Petco reports that business is booming, even with bad reviews like Disgruntled Bunny's.

New research is proving what Petco already learned: peer reviews work. Shoppers are turning to everyday people for product advice. The 2007 Edelman Trust Barometer reports that over half of Americans said they trust "a person like me" for information about a company or product. David Brain, CEO of Edelman, urges companies to stop relying on "top-down communications delivered to an elite audience and move to peer-to-peer dialogue."

Making customer reviews public has an immediate impact on sales and brand loyalty. Data from ForSee Results in 2007 revealed that 40 percent of online shoppers said peer ratings on Web sites influenced their purchasing decisions. Furthermore, this group was 21 percent more satisfied with its purchases than other buyers and was 18 percent more likely to buy from the same site again.

According to Petco executive John Lazarchic, most users who search for products by customer ratings shop longer, buy more, and return less: "The savings in returns alone pays for all the technology involved in the review and ratings feature." And if one product gets too many bad reviews, it usually prompts customers to buy higher-rated, more expensive merchandise instead.

Other advantages? Reviews build camaraderie with an online community where shoppers can connect. They can boost a site's ratings on search sites. And they establish credibility. As long as the reviews aren't overwhelmingly negative, positive reviews have been shown to outweigh the negatives in shoppers' minds. For example, a four-paw review on Petco.com would outnumber one-paw ratings by seven to one.

Lazarchic insists that reviews provide valuable feedback. Critical comments are shared within the company and can instigate changes. In fact, they're finding that the risk is not in receiving too many negative comments on a product, but too few. When no one is responding, it looks like no one is buying it. Or, if they are, they don't care enough about it to talk about it. Petco had that problem at first. In the beginning, when the company posted a small link for users to click and write a review, the silence was deafening. So they added promotional banners to the site and advertised drawings in which lucky reviewers would receive cash prizes. Within a couple of weeks, they'd gotten 4,500 new comments.

Analysts warn that to maintain credibility, reviews shouldn't be edited unless necessary. Petco removes the names of rival brands, URLs, and personal information, but less than 10 percent of the reviews they receive are deleted. Now they're experimenting with the idea of using customer comments as marketing tools in print catalogs, offline ads, e-mail messages, and point-of-purchase displays. In print circulars, for example, Petco highlights its five-paw rated products.

Many of their customers' e-mail addresses are collected through a loyalty program in Petco stores, which means those shoppers may not have visited the Web site. By including customer comments in e-mail ads, it expands the reach of the review program and boosts sales of products those shoppers may not have considered in the store.

According to a Nielsen BuzzMetrics study, the customers most likely to write reviews on Web sites are empty nesters and "young transitionals" without children. Petco found that on their site, reviewers tend to be women with higher levels of education and income who are passionate about their pets. It is generally someone who wants to be helpful, share her opinion, and feel important. Someone, perhaps, like Disgruntled Bunny, who wants to warn others of the dangers of defective travel carriers before another cat escapes.[33]

Questions

1. A customer-centric company builds long-lasting relationships by focusing on what satisfies and retains valuable customers. Discuss how Petco follows this customer-centric philosophy.
2. Go to Petco.com and read some of the customer reviews for various types of products. Do the one- and two-paw ratings tend to outnumber those with four and five paws, or the other way around? Can you find a customer review that Petco could use to market a product in a company circular or e-mail ad?
3. Now that Petco has identified the type of customer most likely to write reviews of their products, discuss the kinds of promotions that might encourage continued loyalty and response online from them in the future. What could they do to appeal to these customers?
4. Many mainstream retailers are still hesitant to post customer reviews on their Web sites. If you were consulting with one of these companies, what arguments would you use to convince management to try them?

Company Clips

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METHOD—SPREADING THE NEWS ABOUT GREEN CLEANING

It is not uncommon for companies to be a bit protective of their brands. As you read in Chapter 10, brand equity and perception are indicators of marketing success. But in today's fast-paced markets, much can be gained by turning ownership of the brand over to consumers. Method is a company that understands the benefits to this risky proposition. Founders Eric Ryan and Adam Lowry created a brand that its customers can take ownership of and have actually built a customer feedback channel that most businesses dream of achieving. Brand advocates, or method's most enthusiastic customers, are the company's most vocal proponents and take an almost evangelical approach to sharing the benefits of green cleaning with the market.

Questions

1. How has method identified customer relationships with the organization? What does the company do to nurture those relationships?
2. Identify the touch points mentioned in the video and list the types of information method could gather at each one.
3. What is the role of technology in method's CRM system?

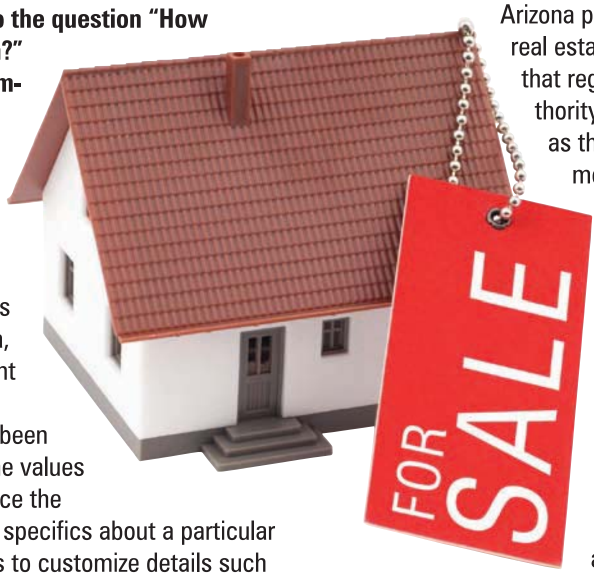
Marketing & You Results

A low score on this poll suggests that you think it is acceptable to complain, whereas a high score suggests you think it is inappropriate to complain, even when you receive a bad product or service. People who perceive complaining to be most acceptable also tend to be aggressive, and those who regard complaining as inappropriate tend to be unassertive and generally passive.

Marketing Miscue

Zillow Product in Possible Violation of State Law

Zillow.com™, operating out of Seattle, Washington (USA), is an online real estate service that was launched in February of 2006. With the name derived from the idea that there are zillions of homes in the marketplace and that people put their heads on pillows in their homes, Zillow's first product offering was a free tool called Zestimate™. Zestimate™ attempts to provide an answer to the question "How much is this home really worth?" by allowing users to create computer-generated estimates of home values.



The Zestimate™ for a particular home is calculated via a proprietary computer program using publicly-available data. The data include sale prices of comparable homes in the area, sales history, and tax assessment information. The median margin-of-error for the Zestimate™ has been around seven percent on all home values that have used the estimate. Since the computer program cannot know specifics about a particular home, the Web site allows users to customize details such as remodeling and upgrades.

With success measured by the Zestimate's usage rate, the company expanded its offerings to include the posting of homes for sale and an overview of recently sold homes. All the user has to do is utilize the location search to access such information. Envisioning the Web site as a type of social network, Zillow later introduced the Make Me Move™ concept. With the Make Me Move™ product, homeowners set a price they cannot refuse just in case someone actually makes them an offer at that price. Ultimately, the company is building the groundwork for a social network that they are calling the Zillow community. According to the company's website, the goal is to create an online community in which homeowners, buyers, sellers, and real estate professionals engage in an exchange of information about homes and neighborhoods.

While an online discussion of real estate might make for more informed buyers and sellers, not all agree that Zillow.com™ has a legitimate product offering. In early 2007, the Arizona Board of Appraisal ordered Zillow to stop offering Zestimate™ as a means of estimating the value of homes in Arizona since Zillow is not a licensed appraiser in that state. The state board issued two cease-and-desist orders to Zillow.com™ before turning the matter over to the criminal division of the state attorney general's office. According to the state board's interpretation of the law, the product is operating as an appraisal according to the law's definition of what constitutes a home appraisal. Zillow executives contend that its estimates are not formal appraisals, since Zestimate™ is just a piece of software that cannot engage actively in the property details. Unfortunately, 25 other states have appraisal laws similar to those in Arizona.

The state board's attempt to shut down Zillow in Arizona prompted much discussion among real estate professionals. Many realtors felt that regulators were overstepping their authority. However, some realtors, as well as the National Community Reinvestment Coalition, felt that the board's actions were justified, citing that the company did not make it obvious that the Zestimate was not an official appraisal and that buyers and sellers were taking the Zestimate too seriously. Apparently, a user had to click on a small blue question mark to receive a pop-up message that said that the Zestimate was not an appraisal and should only be used as a starting point for determining the value of a home.

Zillow was not the only online site offering free home estimates. Sites such as RealEstate.com, RealEstateABC.com, and Reply.com competed with Zillow. However, Zillow was logging more online traffic than these competitors. Although it reported millions of users each month, the company did not receive revenue for its services. Rather, revenue came from online advertising. Thus, a ban in any state would lead to a considerable drop in revenue in the early stages of company growth. Would the company's failure to understand state and local real estate laws result in demise of its key online product offering?

Questions

1. Is Zillow.com™ and its product offerings just a form of online advertising?
2. Are there customer relationships in this type of online transaction?

Critical Thinking Case

You've been ICED!

Scholars at the Woodrow Wilson Center for International Scholars in Washington, D.C. (USA) are hoping to organize and accelerate the adoption of computer games for policy education and exploration. The *Serious Games Initiative* is a building block in an effort to engage a new field of computer and video games applied to non-entertainment purposes. Games for Change (G4C) is a subgroup of the *Serious Games Initiative* that hopes to develop videogame projects by connecting scholars, nonprofit groups, government organizations, companies in the games industry, and individual game developers/artists. Through this network of players, G4C hopes to support new uses for digital gaming.

One such video game receiving considerable attention is "ICED!" which is a play on the acronym for the Department of Homeland Security's Immigration and Customs Enforcement office. "ICED! I Can End Deportation" is a downloadable, interactive 3D role-playing video. Targeted to high school and college age students, ICED! allows players to become engaged actively in the immigration debate by experiencing life as an immigrant who has run afoul of the U.S. immigration system. The game was created and designed by Heidi Boisvert and Natalia Rodriguez (MFA students in the Integrated Media Arts Program at Hunter College and the Performance and Interactive Media Arts Program at Brooklyn College respectively) in partnership with Breakthrough (a New York based human rights organization).

The goal of ICED! is to condemn the 1996 U.S. immigration laws. The game attempts to teach players that the Illegal Immigration Reform and Immigrant Responsibility Act (IIRIRA) passed in 1996 is too harsh and denies due process while violating fundamental human rights. As such, ICED! gamers can play as one of several immigrant characters, all of whom were created based on real situations. Each of the characters has different immigration status and ethnicity so as to dispel ideas that the majority of immigrants are Mexican and that only undocumented immigrants are being detained and deported. ICED! gamers can become a Japanese computer science student who loses his student visa because he fails to take a full load of university classes, a 10th-grade Indian girl who has a green card but is detained because of the high school essay she wrote on the Department of Homeland Security, a 16-year old New York girl from Guinea accused of planning a suicide bombing and detained for six weeks before the charges were dropped, a Haitian war veteran facing deportation after turning to a life of alcohol and crime upon returning from Iraq, or a Mexican who graduated from high school in the United States but whose family overstayed its visa.

The game, which takes anywhere from 10 to 30 minutes to play, has two levels. In the first level, the city, the player is given 100 points. Points are gained by answering myth/fact questions about immigration correctly and by doing good deeds in the community, all while avoiding immigration officers. Not only do incorrect answers result in a loss of points, incorrect answers also mean that the player is chased by more and more immigration officers. Earning points can delay detention, but once a player reaches level two of the game, detention is inevitable. In detention, the player has to answer more myth/fact questions and is confronted by moral choices (e.g., Do you jump the turnstile at the subway or pay the fare?). Again, wrong decisions result in a loss of points and, ultimately, deportation.

As a human rights organization, Breakthrough believes that immigration laws are arbitrary. Through the ICED! online game, Breakthrough seeks to promote its own agenda and influence public opinion. Other organizations are also using video games to highlight particular causes:

- "Darfur is Dying" simulates a Sudanese refugee camp.
- "La Migra" portrays an immigration agent who either receives praise for stopping illegal border crossing or a termination notice if too many illegals cross over.
- "Peacemaker" allows players to act as both Israeli and Palestinian leaders seeking to diffuse tension in the Middle East.

But, is there a market for games that explain social and political issues? And if so, do nonprofit organizations have the resources to gain widespread distribution? Will computer and video games such as these displace board games on family game night or popular games of the Halo genre? Is there a true marketplace opportunity here, or will the games merely supplement the tools used currently for advocacy and educational causes?

Questions

1. Are there any privacy concerns related to capturing user information via cause-related online computer games?
2. What type of competition do these advocacy-based games face?

ANATOMY OF A Customer Relations Decision

Sports Team

The National Basketball Association uses its YouTube channel as a touchpoint to engage with fans.

1 Customer-centric site fosters enthusiasm for the sport.

2 Official NBA footage provides exciting games for fans worldwide.

3 Fans subscribe and submit their own videos, sharing their information with the NBA.

4 Link to NBA.com encourages further interaction and the purchase of official gear.

GLOSSARY

3PL See *third-party logistics firm.*

80/20 principle A principle holding that 20 percent of all customers generate 80 percent of the demand.

A

ABC segmentation The supply-chain process whereby customers are placed into groups A, B, and C according to their overall long-term value to the firm and to the extent to which the firm can serve their desires.

accelerator principle See *multiplier effect.*

accessory equipment Goods, such as portable tools and office equipment, that are less expensive and shorter-lived than major equipment.

activity-based costing (ABC) An accounting method used in measurement integration to assess the costs associated with each supply chain activity.

adopter A consumer who was happy enough with his or her trial experience with a product to use it again.

advergaming Placing advertising messages in Web-based or video games to advertise or promote a product, service, organization, or issue.

advertising Impersonal, one-way mass communication about a product or organization that is paid for by a marketer.

advertising appeal A reason for a person to buy a product.

advertising campaign A series of related advertisements focusing on a common theme, slogan, and set of advertising appeals.

advertising objective A specific communication task that a campaign should accomplish for a specified target audience during a specified period.

advertising response function A phenomenon in which spending for advertising and sales promotion increases sales or market share up to a certain level but then produces diminishing returns.

advocacy advertising A form of advertising in which an organization expresses its views on controversial issues or responds to media attacks.

agents and brokers Wholesaling intermediaries who do not take title to a product but facilitate its sale from producer to end user by representing retailers, wholesalers, or manufacturers.

agile supply chain management The supply chain strategy that focuses primarily on the ability of the firm to fulfill customer demand, even if this means somewhat higher costs.

AIDA concept A model that outlines the process for achieving promotional goals in terms of stages of consumer involvement with the message; the acronym stands for attention, interest, desire, and action.

applied research An attempt to develop new or improved products.

Arm's Length relationship A relationship between companies that is loose, characterized by low relational investment and trust, and usually taking the form of a series of discrete transactions with no/low expectation of future interaction or service.

aspirational reference group A group that someone would like to join.

assurance The knowledge and courtesy of employees and their ability to convey trust.

ATC See *average total cost.*

atmosphere The overall impression conveyed by a store's physical layout, decor, and surroundings.

attitude A learned tendency to respond consistently toward a given object.

audience selectivity The ability of an advertising medium to reach a precisely defined market.

automatic replenishment program An inventory management system that triggers shipments only once a good is sold to the customer; the program uses EDI linkage connected with barcode scanners at the point of purchase, so the supplier can view the inventory being held at the next tier of the supply chain in real time.

automatic vending The use of machines to offer goods for sale.

AVC See *average variable cost.*

average total cost (ATC) Total costs divided by quantity of output.

average variable cost (AVC) Total variable costs divided by quantity of output.

B

baby boomers People born between 1946 and 1964.

bait pricing A price tactic that tries to get consumers into a store through false or misleading price advertising and then uses high-pressure selling to persuade consumers to buy more expensive merchandise.

Balanced Scorecard Approach A measurement system used to evaluate overall supply chain performance.

bar codes See *universal product codes.*

base price The general price level at which the company expects to sell the good or service.

basic research Pure research that aims to confirm an existing theory or to learn more about a concept or phenomenon.

basing-point pricing A price tactic that charges freight from a given (basing) point, regardless of the city from which the goods are shipped.

behavioral targeting A form of observation marketing research that uses data mining coupled with identifying Web surfers by their IP addresses plus demographic/psychographic profiles.

BehaviorScan A scanner-based research program that tracks the purchases of 3,000 households through store scanners in each research market.

belief An organized pattern of knowledge that an individual holds as true about his or her world.
benchmarks The standards set by measuring the best, quickest, and most efficient work practices.
benefit segmentation The process of grouping customers into market segments according to the benefits they seek from the product.
brainstorming The process of getting a group to think of unlimited ways to vary a product or solve a problem.
brand A name, term, symbol, design, or combination thereof that identifies a seller's products and differentiates them from competitors' products.
brand equity The value of company and brand names.
brand loyalty A consistent preference for one brand over all others.
brand mark The elements of a brand that cannot be spoken.
brand name That part of a brand that can be spoken, including letters, words, and numbers.
break-even analysis A method of determining what sales volume must be reached before total revenue equals total costs.
build-to-order See *mass customization.*
business analysis The second stage of the screening process where preliminary figures for demand, cost, sales, and profitability are calculated.
business marketing The marketing of goods and services to individuals and organizations for purposes other than personal consumption.
business process Bundles of interconnected activities that stretch across firms in the supply chain.
business product (industrial product) A product used to manufacture other goods or services, to facilitate an organization's operations, or to resell to other customers.
business services Expense items that do not become part of a final product.
business-to-business electronic commerce The use of the Internet to facilitate the exchange of goods, services, and information between organizations.
business-to-business online exchange An electronic trading floor that provides companies with integrated links to their customers and suppliers.
buyer A department head who selects the merchandise for his or her department and may also be responsible for promotion and personnel.
buyer for export An intermediary in the global market that assumes all ownership risks and sells globally for its own account.
buying center All those persons in an organization who become involved in the purchase decision.

C

CAFTA See *Central America Free Trade Agreement.*
campaign management Developing product or service offerings customized for the appropriate customer segment and then pricing and communicating these offerings for the purpose of enhancing customer relationships.
cannibalization A situation that occurs when sales of a new product cut into sales of a firm's existing products.
capital-intensive Using more capital than labor in the production process.
cash cow In the portfolio matrix, a business unit that usually generates more cash than it needs to maintain its market share.
cash discount A price reduction offered to a consumer, an industrial user, or a marketing intermediary in return for prompt payment of a bill.
casuist ethical theory A theory that compares a current ethical dilemma with examples of similar ethical dilemmas and their outcomes.
category killers Specialty discount stores that heavily dominate their narrow merchandise segment.
cause-related marketing A type of sponsorship involving the association of a for-profit company and a nonprofit organization; through the sponsorship, the company's product or service is promoted, and money is raised for the nonprofit.
cause-related marketing The cooperative marketing efforts between a "for-profit" firm and a "nonprofit organization."
Central America Free Trade Agreement (CAFTA) A trade agreement, instituted in 2005, that includes Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and the United States.
central-location telephone (CLT) facility A specially designed phone room used to conduct telephone interviewing.
CGM See *consumer generated media.*
chain stores Stores owned and operated as a group by a single organization.
channel A medium of communication—such as a voice, radio, or newspaper—for transmitting a message.
channel captain See *channel leader.*
channel conflict A clash of goals and methods between distribution channel members.
channel control A situation that occurs when one marketing channel member intentionally affects another member's behavior.
channel cooperation See *channel partnering.*
channel leader (channel captain) A member of a marketing channel that exercises authority and power over the activities of other channel members.
channel members All parties in the marketing channel that negotiate with one another, buy and sell products, and facilitate the change of ownership between buyer and seller in the course of moving the product from the manufacturer into the hands of the final consumer.
channel of distribution See *marketing channel.*
channel partnering (channel cooperation) The joint effort of all channel members to create a channel that serves customers and creates a competitive advantage.
channel power The capacity of a particular marketing channel member to control or influence the behavior of other channel members.
CI See *competitive intelligence.*
closed-ended question An interview question that asks the respondent to make a selection from a limited list of responses.
CLT See *central-location telephone facility.*
cobranding Placing two or more brand names on a product or its package.
code of ethics A guideline to help marketing managers and other employees make better decisions.
cognitive dissonance Inner tension that a consumer experiences after recognizing an inconsistency between behavior and values or opinions.
commercialization The decision to market a product.
communication The process by which we exchange or share meanings through a common set of symbols.

comparative advertising A form of advertising that compares two or more specifically named or shown competing brands on one or more specific attributes.
competitive advantage One or more unique aspects of an organization that cause target consumers to patronize that firm rather than competitors.
competitive advantage The set of unique features of a company and its products that are perceived by the target market as significant and superior to the competition.
competitive advertising A form of advertising designed to influence demand for a specific brand.
competitive intelligence (CI) An intelligence system that helps managers assess their competition and vendors in order to become more efficient and effective competitors.
compiled list A customer list that was developed by gathering names and addresses from telephone directories and membership rosters, usually enhanced with information from public records, such as census data, auto registrations, birth announcements, business start-ups, or bankruptcies.
component lifestyles The practice of choosing goods and services that meet one's diverse needs and interests rather than conforming to a single, traditional lifestyle.
component parts Either finished items ready for assembly or products that need very little processing before becoming part of some other product.
computer-assisted personal interviewing An interviewing method in which the interviewer reads the questions from a computer screen and enters the respondent's data directly into the computer.
computer-assisted self-interviewing An interviewing method in which a mall interviewer intercepts and directs willing respondents to nearby computers where the respondent reads questions off a computer screen and directly keys his or her answers into a computer.
concentrated targeting strategy A strategy used to select one segment of a market for targeting marketing efforts.
concept test A test to evaluate a new-product idea, usually before any prototype has been created.
consideration set See *evoked set*.
consultative selling See *relationship selling*.
consumer behavior Processes a consumer uses to make purchase decisions, as well as to use and dispose of purchased goods or services; also includes factors that influence purchase decisions and product use.
consumer decision-making process A five-step process used by consumers when buying goods or services.
consumer generated media (CGM) Media which is consumer generated and shared with other consumers.
consumer penalty An extra fee paid by the consumer for violating the terms of the purchase agreement.
consumer product A product bought to satisfy an individual's personal wants.
Consumer Product Safety Commission (CPSC) A federal agency established to protect the health and safety of consumers in and around their homes.
consumer sales promotion Sales promotion activities targeting the ultimate consumer.
continuous media schedule A media scheduling strategy in which advertising is run steadily throughout the advertising period; used for products in the latter stages of the product life cycle.
contract logistics See *outsourcing*.
contract manufacturing Private-label manufacturing by a foreign company.
control Provides the mechanisms for evaluating marketing results in light of the plan's objectives and for correcting actions that do not help the organization reach those objectives within budget guidelines.
convenience product A relatively inexpensive item that merits little shopping effort.
convenience sample A form of nonprobability sample using respondents who are convenient or readily accessible to the researcher—for example, employees, friends, or relatives.
convenience store A miniature supermarket, carrying only a limited line of high-turnover convenience goods.
cooperative advertising An arrangement in which the manufacturer and the retailer split the costs of advertising the manufacturer's brand.
cooperative relationship A relationship between companies that takes the form of informal partnership with moderate levels of trust and information sharing as needed to further each company's goals.
core service The most basic benefit the consumer is buying.
corporate blogs Blogs that are sponsored by a company or one of its brands and maintained by one or more of the company's employees.
corporate social responsibility Business's concern for society's welfare.
cost competitive advantage Being the low-cost competitor in an industry while maintaining satisfactory profit margins.
cost per contact The cost of reaching one member of the target market.
countertrade A form of trade in which all or part of the payment for goods or services is in the form of other goods or services.
coupon A certificate that entitles consumers to an immediate price reduction when they buy the product.
CPSC See *Consumer Product Safety Commission*.
credence quality A characteristic that consumers may have difficulty assessing even after purchase because they do not have the necessary knowledge or experience.
crisis management A coordinated effort to handle all the effects of unfavorable publicity or of another unexpected unfavorable event.
CRM See *customer relationship management*.
cross-tabulation A method of analyzing data that lets the analyst look at the responses to one question in relation to the responses to one or more other questions.
culture The set of values, norms, attitudes, and other meaningful symbols that shape human behavior, and the artifacts, or products, of that behavior as they are transmitted from one generation to the next.
cumulative quantity discount A deduction from list price that applies to the buyer's total purchases made during a specific period.
customer integration A competency that enables firms to offer long-lasting, distinctive, value-added offerings to those customers who represent the greatest value to the firm or supply chain.

customer relationship management (CRM) A company-wide business strategy designed to optimize profitability, revenue, and customer satisfaction by focusing on highly defined and precise customer groups.

customer relationship management process The prioritization of a firm's marketing focus on different customer groups according to each group's long-term value to the company or supply chain; designed to identify and build relationships with good customers.

customer satisfaction Customers' evaluation of a good or service in terms of whether it has met their needs and expectations.

customer service management process A multi-company, unified response system to the customer whenever complaints, concerns, questions, or comments are voiced; designed to ensure that customer relationships remain strong.

customer value The relationship between benefits and the sacrifice necessary to obtain those benefits.

customer-centric A philosophy under which the company customizes its product and service offering based on data generated through interactions between the customer and the company.

D

data warehouse A central repository for data from various functional areas of the organization that are stored and inventoried on a centralized computer system so that the information can be shared across all functional departments of the business.

database A collection of data, especially one that can be accessed and manipulated by computer software.

database marketing The creation of a large computerized file of customers' and potential customers' profiles and purchase patterns.

decision support system (DSS) An interactive, flexible computerized information system that enables managers to obtain and manipulate information as they are making decisions.

decline stage The fourth stage of the product life cycle, characterized by a long-run drop in sales.

decoding Interpretation of the language and symbols sent by the source through a channel.

delayed-quotation pricing A price tactic used for industrial installations and many accessory items, in which a firm price is not set until the item is either finished or delivered.

demand The quantity of a product that will be sold in the market at various prices for a specified period.

demand management process The alignment of supply and demand throughout the supply chain to anticipate customer requirements at each level and create demand-related plans of action prior to actual customer purchasing behavior.

demographic segmentation Segmenting markets by age, gender, income, ethnic background, and family life cycle.

demography The study of people's vital statistics, such as their age, race and ethnicity, and location.

deontological theory A theory that states that people should adhere to their obligations and duties when analyzing an ethical dilemma.

department store A store housing several departments under one roof.

derived demand The demand for business products.

destination stores Stores that consumers purposefully plan to visit.

development The stage in the product development process in which a prototype is developed and a marketing strategy is outlined.

diffusion The process by which the adoption of an innovation spreads.

direct channel A distribution channel in which producers sell directly to consumers.

direct foreign investment Active ownership of a foreign company or of overseas manufacturing or marketing facilities.

direct marketing (direct-response marketing) Techniques used to get consumers to make a purchase from their home, office, or another nonretail setting.

direct retailing The selling of products by representatives who work door-to-door, office-to-office, or at home parties.

direct-response marketing See *direct marketing*.

discount store A retailer that competes on the basis of low prices, high turnover, and high volume.

discrepancy of assortment The lack of all the items a customer needs to receive full satisfaction from a product or products.

discrepancy of quantity The difference between the amount of product produced and the amount an end user wants to buy.

disintermediation The elimination of intermediaries such as wholesalers or distributors from a marketing channel.

distribution resource planning (DRP) An inventory control system that manages the replenishment of goods from the manufacturer to the final consumer.

diversification A strategy of increasing sales by introducing new products into new markets.

dog In the portfolio matrix, a business unit that has low growth potential and a small market share.

DRP See *distribution resource planning*.

drugstore A retail store that stocks pharmacy-related products and services as its main draw.

DSS See *decision support system*.

dual distribution (multiple distribution) The use of two (or more) channels to distribute the same product to target markets.

dumping The sale of an exported product at a price lower than that charged for the same or a like product in the "home" market of the exporter.

E

EDI See *electronic data interchange*.

elastic demand A situation in which consumers buy significantly more or less of a product when its price changes.

elasticity of demand Consumers' responsiveness or sensitivity to changes in price.

electronic data interchange (EDI) Information technology that replaces the paper documents that usually accompany business transactions, such as purchase orders and invoices, with electronic transmission of the needed information to reduce inventory levels, improve cash flow, streamline operations, and increase the speed and accuracy of information transmission.

electronic distribution A distribution technique that includes any kind of product or service that can be distributed electronically, whether over traditional forms such as fiber-optic cable or through satellite transmission of electronic signals.

empathy Caring, individualized attention to customers.

empowerment Delegation of authority to solve customers' problems quickly—usually by the first person that the customer notifies regarding a problem.

encoding The conversion of a sender's ideas and thoughts into a message, usually in the form of words or signs.

environmental management When a company implements strategies that attempt to shape the external environment within which it operates.

environmental scanning Collection and interpretation of information about forces, events, and relationships in the external environment that may affect the future of the organization or the implementation of the marketing plan.

escalator pricing A price tactic in which the final selling price reflects cost increases incurred between the time the order is placed and the time delivery is made.

ethics The moral principles or values that generally govern the conduct of an individual.

ethnographic research The study of human behavior in its natural context; involves observation of behavior and physical setting.

European Union A free trade zone encompassing 27 European countries.

evaluation Gauging the extent to which the marketing objectives have been achieved during the specified time period.

evoked set (consideration set) A group of brands, resulting from an information search, from which a buyer can choose.

exchange People giving up something to receive something they would rather have.

exclusive distribution A form of distribution that establishes one or a few dealers within a given area.

executive interviews A type of survey that involves interviewing businesspeople at their offices concerning industrial products or services.

experience curves Curves that show costs declining at a predictable rate as experience with a product increases.

experience quality A characteristic that can be assessed only after use.

experiment A method a researcher uses to gather primary data that alters one or more variables while observing the effect on another variable (typically sales).

export agent An intermediary who acts like a manufacturer's agent for the exporter. The export agent lives in the foreign market.

export broker An intermediary who plays the traditional broker's role by bringing buyer and seller together.

exporting Selling domestically produced products to buyers in another country.

express warranty A written guarantee.

extensive decision making The most complex type of consumer decision making, used when buying an unfamiliar, expensive product or an infrequently bought item; requires use of several criteria for evaluating options and much time for seeking information.

external information search The process of seeking information in the outside environment.

F

factory outlet An off-price retailer that is owned and operated by a manufacturer.

family brand Marketing several different products under the same brand name.

family life cycle (FLC) A series of stages determined by a combination of age, marital status, and the presence or absence of children.

FDA See *Food and Drug Administration.*

Federal Trade Commission (FTC) A federal agency empowered to prevent persons or corporations from using unfair methods of competition in commerce.

feedback The receiver's response to a message.

field service firm A firm that specializes in interviewing respondents on a subcontracted basis.

fixed cost A cost that does not change as output is increased or decreased.

FLC See *family life cycle.*

flexible pricing (variable pricing) A price tactic in which different customers pay different prices for essentially the same merchandise bought in equal quantities.

flighted media schedule A media scheduling strategy in which ads are run heavily every other month or every two weeks, to achieve a greater impact with an increased frequency and reach at those times.

floating exchange rates Prices of different currencies move up and down based on the demand for and the supply of each currency.

FOB origin pricing A price tactic that requires the buyer to absorb the freight costs from the shipping point ("free on board").

focus group Seven to ten people who participate in a group discussion led by a moderator.

follow-up The final step of the selling process, in which the salesperson ensures that delivery schedules are met, that the goods or services perform as promised, and that the buyers' employees are properly trained to use the products.

Food and Drug Administration (FDA) A federal agency charged with enforcing regulations against selling and distributing adulterated, misbranded, or hazardous food and drug products.

Foreign Corrupt Practices Act A law that prohibits U.S. corporations from making illegal payments to public officials of foreign governments to obtain business rights or to enhance their business dealings in those countries.

four Ps Product, place, promotion, and price, which together make up the marketing mix.

frame error An error that occurs when a sample drawn from a population differs from the target population.

franchise The right to operate a business or to sell a product.

franchisee An individual or business that is granted the right to sell another party's product.

franchisor The originator of a trade name, product, methods of operation, and so on, that grants operating rights to another party to sell its product.

freight absorption pricing A price tactic in which the seller pays all or part of the actual freight charges and does not pass them on to the buyer.

frequency The number of times an individual is exposed to a given message during a specific period.

frequent buyer program A loyalty program in which loyal consumers are rewarded for making multiple purchases of a particular good or service.

FTC See *Federal Trade Commission.*

full-line discount stores A retailer that offers consumers very limited service and carries a broad assortment of well-known, nationally branded "hard goods."

functional discount (trade discount) A discount to wholesalers and retailers for performing channel functions.

G

gap model A model identifying five gaps that can cause problems in service delivery and influence customer evaluations of service quality.

GATT See *General Agreement on Tariffs and Trade*.

General Agreement on Tariffs and Trade (GATT) A trade agreement that contained loopholes that enabled countries to avoid trade-barrier reduction agreements.

Generation X People born between 1965 and 1978.

Generation Y People born between 1979 and 1994.

generic product A no-frills, no-brand-name, low-cost product that is simply identified by its product category.

generic product name Identifies a product by class or type and cannot be trademarked.

geodemographic segmentation Segmenting potential customers into neighborhood lifestyle categories.

geographic segmentation Segmenting markets by region of a country or the world, market size, market density, or climate.

global brand A brand where at least one-third of the product is sold outside its home country or region.

global marketing Individuals and organizations using a global vision to effectively market goods and services across national boundaries.

global marketing standardization Production of uniform products that can be sold the same way all over the world.

global vision Recognizing and reacting to international marketing opportunities, using effective global marketing strategies, and being aware of threats from foreign competitors in all markets.

gross margin The amount of money the retailer makes as a percentage of sales after the cost of goods sold is subtracted.

group dynamics Group interaction essential to the success of focus-group research.

growth stage The second stage of the product life cycle when sales typically grow at an increasing rate, many competitors enter the market, large companies may start acquiring small pioneering firms, and profits are healthy.

H

heterogeneity The variability of the inputs and outputs of services, which causes services to tend to be less standardized and less uniform than goods.

horizontal conflict A channel conflict that occurs among channel members on the same level.

horizontal position One of three dimensions of supply chain network design; the position of a firm, relative to other firms, along the supply chain.

horizontal structure One of three dimensions of supply chain network design; the number of tiers (columns) in the supply chain, representing the total number of levels through which goods and services must pass from the earliest to end stages of the chain.

I

ideal self-image The way an individual would like to be.

IMC See *integrated marketing communications*.

IMF See I*nternational Monetary Fund*.

implementation The process that turns a marketing plan into action assignments and ensures that these assignments are executed in a way that accomplishes the plan's objectives.

implied warranty An unwritten guarantee that the good or service is fit for the purpose for which it was sold.

independent retailers Retailers owned by a single person or partnership and not operated as part of a larger retail institution.

individual branding Using different brand names for different products.

industrial product See *business product*.

inelastic demand A situation in which an increase or a decrease in price will not significantly affect demand for the product.

inflation A measure of the decrease in the value of money, expressed as the percentage reduction in value since the previous year.

infomercial A 30-minute or longer advertisement that looks more like a TV talk show than a sales pitch.

informational labeling A type of package labeling designed to help consumers make proper product selections and lower their cognitive dissonance after the purchase.

InfoScan A scanner-based sales-tracking service for the consumer packaged-goods industry.

innovation A product perceived as new by a potential adopter.

inseparability The inability of the production and consumption of a service to be separated. Consumers must be present during the production.

installations See *major equipment*.

institutional advertising A form of advertising designed to enhance a company's image rather than promote a particular product.

intangibility The inability of services to be touched, seen, tasted, heard, or felt in the same manner that goods can be sensed.

integrated marketing communications (IMC) The careful coordination of all promotional messages for a product or a service to assure the consistency of messages at every contact point where a company meets the consumer.

integrated relationship A relationship between companies that is tightly connected, with linked processes across and between firm boundaries, and high levels of trust and interfirm commitment.

intensive distribution A form of distribution aimed at having a product available in every outlet where target customers might want to buy it.

interaction The point at which a customer and a company representative exchange information and develop learning relationships.

internal information search The process of recalling past information stored in the memory.

internal marketing Treating employees as customers and developing systems and benefits that satisfy their needs.

internal operations integration Links internally performed work into a seamless process that stretches across departmental and/or functional boundaries, with the goal of satisfying customer requirements.

International Monetary Fund (IMF) An international organization that acts as a lender of last resort, providing loans to troubled nations, and also works to promote trade through financial cooperation.

interpersonal communication Direct, face-to-face communication between two or more people.

GLOSSARY

introductory stage The first stage of the product life cycle in which the full-scale launch of a new product into the marketplace occurs.

inventory control system A method of developing and maintaining an adequate assortment of materials or products to meet a manufacturer's or a customer's demand.

involvement The amount of time and effort a buyer invests in the search, evaluation, and decision processes of consumer behavior.

J

JIT See *just-in-time production*.

joint costs Costs that are shared in the manufacturing and marketing of several products in a product line.

joint demand The demand for two or more items used together in a final product.

joint venture When a domestic firm buys part of a foreign company or joins with a foreign company to create a new entity.

just-in-time production (JIT) A process that redefines and simplifies manufacturing by reducing inventory levels and delivering raw materials just when they are needed on the production line.

K

keiretsu A network of interlocking corporate affiliates.

keystoning The practice of marking up prices by 100 percent, or doubling the cost.

knowledge management The process by which learned information from customers is centralized and shared in order to enhance the relationship between customers and the organization.

L

laboratory market testing See *simulated market testing*.

lead generation (prospecting) Identification of those firms and people most likely to buy the seller's offerings.

lead qualification Determination of a sales prospect's (1) recognized need, (2) buying power, and (3) receptivity and accessibility.

leader pricing (loss-leader pricing) A price tactic in which a product is sold near or even below cost in the hope that shoppers will buy other items once they are in the store.

Leagile supply chain management A supply chain management strategy that combines the best elements of the lean and agile strategies for a particular product/market combination.

lean supply chain management The strategy that focuses primarily on the removal of waste from the supply chain to achieve the lowest total cost to the members of the supply chain system.

learning A process that creates changes in behavior, immediate or expected, through experience and practice.

learning (Ch.21 CRM) An informal process of collecting customer data through customer comments and feedback on product or service performance.

licensing The legal process whereby a licensor agrees to let another firm use its manufacturing process, trademarks, patents, trade secrets, or other proprietary knowledge.

lifestyle A mode of living as identified by a person's activities, interests, and opinions.

lifetime value analysis (LTV) A data manipulation technique that projects the future value of the customer over a period of years using the assumption that marketing to repeat customers is more profitable than marketing to first-time buyers.

limited decision making The type of decision making that requires a moderate amount of time for gathering information and deliberating about an unfamiliar brand in a familiar product category.

logistics The efficient and cost-effective forward and reverse flow as well as storage of goods, services, and related information, into, through, and out of channel member companies. Logistics functions typically include transportation and storage of assets, as well as their sorting, accumulation, consolidation, and/or allocation for the purpose of meeting customer requirements.

logistics information system The link that connects all of the logistics components of the supply chain.

loss-leader pricing See *leader pricing*.

loyalty marketing program A promotional program designed to build long-term, mutually beneficial relationships between a company and its key customers.

LTV See *lifetime value analysis*.

M

major equipment (installations) Capital goods such as large or expensive machines, mainframe computers, blast furnaces, generators, airplanes, and buildings.

mall intercept interview A survey research method that involves interviewing people in the common areas of shopping malls.

management decision problem A broad-based problem that uses marketing research in order for managers to take proper actions.

manufacturer's brand The brand name of a manufacturer.

manufacturing flow management process A process that ensures that firms in the supply chain have the resources they need.

marginal cost (MC) The change in total costs associated with a one-unit change in output.

marginal revenue (MR) The extra revenue associated with selling an extra unit of output or the change in total revenue with a one-unit change in output.

markdown money A payment by a manufacturer to a retailer to help cover the costs of markdowns that the retailer had to take.

market People or organizations with needs or wants and the ability and willingness to buy.

market development A marketing strategy that entails attracting new customers to existing products.

market opportunity analysis (MOA) The description and estimation of the size and sales potential of market segments that are of interest to the firm and the assessment of key competitors in these market segments.

market orientation A philosophy that assumes that a sale does not depend on an aggressive sales force but rather on a customer's decision to purchase a product. It is synonymous with the marketing concept.

market penetration A marketing strategy that tries to increase market share among existing customers.

market segment A subgroup of people or organizations sharing one or more characteristics that cause them to have similar product needs.

market segmentation The process of dividing a market into meaningful, relatively similar, and identifiable segments or groups.

market share A company's product sales as a percentage of total sales for that industry.

marketing The activity, set of institutions, and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large.

marketing audit A thorough, systematic, periodic evaluation of the objectives, strategies, structure, and performance of the marketing organization.

marketing channel (channel of distribution) A set of interdependent organizations that ease the transfer of ownership as products move from producer to business user or consumer.

marketing concept The idea that the social and economic justification for an organization's existence is the satisfaction of customer wants and needs while meeting organizational objectives.

marketing information Everyday information about developments in the marketing environment that managers use to prepare and adjust marketing plans.

marketing mix A unique blend of product, place, promotion, and pricing strategies designed to produce mutually satisfying exchanges with a target market.

marketing myopia Defining a business in terms of goods and services rather than in terms of the benefits that customers seek.

marketing objective A statement of what is to be accomplished through marketing activities.

marketing plan A written document that acts as a guidebook of marketing activities for the marketing manager.

marketing planning Designing activities relating to marketing objectives and the changing marketing environment.

marketing research The process of planning, collecting, and analyzing data relevant to a marketing decision.

marketing research aggregator A company that acquires, catalogs, reformats, segments, and resells reports already published by marketing research firms.

marketing research objective The specific information needed to solve a marketing research problem; the objective should be to provide insightful decision-making information.

marketing research problem Determining what information is needed and how that information can be obtained efficiently and effectively.

marketing strategy The activities of selecting and describing one or more target markets and developing and maintaining a marketing mix that will produce mutually satisfying exchanges with target markets.

marketing-controlled information source A product information source that originates with marketers promoting the product.

markup pricing The retail cost of a product determined by adding the cost from the producer plus amounts for profit and for expenses not otherwise accounted for.

Maslow's hierarchy of needs A method of classifying human needs and motivations into five categories in ascending order of importance: physiological, safety, social, esteem, and self-actualization.

mass communication The communication of a concept or message to large audiences.

mass customization (build-to-order) A production method whereby products are not made until an order is placed by the customer; products are made according to customer specifications.

mass customization A strategy that uses technology to deliver customized services on a mass basis.

mass merchandising A retailing strategy using moderate to low prices on large quantities of merchandise and lower service to stimulate high turnover of products.

material and service supplier integration The strategic alignment between a firm and their supply chain materials and services providers that enables the firm to streamline work processes and provide smooth, high-quality customer experiences.

materials management See *materials requirement planning.*

materials requirement planning (MRP) (materials management) An inventory control system that manages the replenishment of raw materials, supplies, and components from the supplier to the manufacturer.

materials-handling system A method of moving inventory into, within, and out of the warehouse.

maturity stage The third stage of the product life cycle during which sales increase at a decreasing rate.

MC See *marginal cost.*

measurement error An error that occurs when there is a difference between the information desired by the researcher and the information provided by the measurement process.

measurement integration The performance assessment of the supply chain as a whole that also holds each individual firm or business unit accountable for meeting its own goals.

media mix The combination of media to be used for a promotional campaign.

media planning The series of decisions advertisers make regarding the selection and use of media, allowing the marketer to optimally and cost-effectively communicate the message to the target audience.

media schedule Designation of the media, the specific publications or programs, and the insertion dates of advertising.

medium The channel used to convey a message to a target market.

merchant wholesaler An institution that buys goods from manufacturers and resells them to businesses, government agencies, and other wholesalers or retailers and that receives and takes title to goods, stores them in its own warehouses, and later ships them.

Mercosur The largest Latin American trade agreement; includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, and Uruguay.

metrics Standard measures that can be used repeatedly to assess performance on a supply chain-related process.

mission statement A statement of the firm's business based on a careful analysis of benefits sought by present and potential customers and an analysis of existing and anticipated environmental conditions.

MOA See *market opportunity analysis.*

modified rebuy A situation where the purchaser wants some change in the original good or service.

moral relativists Persons who believe that ethical truths depend on the individuals and groups holding them.

morals The rules people develop as a result of cultural values and norms.

motive A driving force that causes a person to take action to satisfy specific needs.

MR See *marginal revenue.*

MRP See *materials requirement planning.*

multiculturalism When all major ethnic groups in an area—such as a city, county, or census tract—are roughly equally represented.

multinational corporation A company that is heavily engaged in international trade, beyond exporting and importing.

multiple distribution See *dual distribution*.

multiplier effect (accelerator principle) Phenomenon in which a small increase or decrease in consumer demand can produce a much larger change in demand for the facilities and equipment needed to make the consumer product.

multisegment targeting strategy A strategy that chooses two or more well-defined market segments and develops a distinct marketing mix for each.

mystery shoppers Researchers posing as customers who gather observational data about a store.

N

NAFTA See *North American Free Trade Agreement*.

NAICS See *North American Industry Classification System*.

need recognition Result of an imbalance between actual and desired states.

needs assessment A determination of the customer's specific needs and wants, and the range of options the customer has for satisfying them.

negotiation The process during which both the salesperson and the prospect offer special concessions in an attempt to arrive at a sales agreement.

networking A process of finding out about potential clients from friends, business contacts, coworkers, acquaintances, and fellow members in professional and civic organizations.

new buy A situation requiring the purchase of a product for the first time.

new product A product new to the world, the market, the producer, the seller, or some combination of these.

new-product strategy A plan that links the new-product development process with the objectives of the marketing department, the business unit, and the corporation.

niche One segment of a market.

niche competitive advantage The advantage achieved when a firm seeks to target and effectively serve a small segment of the market.

noise Anything that interferes with, distorts, or slows down the transmission of information.

nonaspirational reference group A group with which an individual does not want to associate.

noncorporate blogs Independent blogs that are not associated with the marketing efforts of any particular company or brand.

noncumulative quantity discount A deduction from list price that applies to a single order rather than to the total volume of orders placed during a certain period.

nonmarketing-controlled information source A product information source that is not associated with advertising or promotion.

nonprobability sample Any sample in which little or no attempt is made to get a representative cross section of the population.

nonprofit organization An organization that exists to achieve some goal other than the usual business goals of profit, market share, or return on investment.

nonprofit organization marketing The effort by nonprofit organizations to bring about mutually satisfying exchanges with target markets.

nonstore retailing Selling to customers through other means than by visiting a store.

norm A value or attitude deemed acceptable by a group.

North American Free Trade Agreement (NAFTA) An agreement between Canada, the United States, and Mexico to reduce trade barriers between the countries.

North American Industry Classification System (NAICS) A detailed numbering system developed by the United States, Canada, and Mexico to classify North American business establishments by their main production processes.

O

observation research A research method that relies on four types of observation: people watching people, people watching an activity, machines watching people, and machines watching an activity.

odd-even pricing (psychological pricing) A price tactic that uses odd-numbered prices to connote bargains and even-numbered prices to imply quality.

OEMs See *original equipment manufacturers*.

off-price retailer A retailer that sells at prices 25 percent or more below traditional department store prices because it pays cash for its stock and usually doesn't ask for return privileges.

one-to-one marketing An individualized marketing method that utilizes customer information to build long-term, personalized, and profitable relationships with each customer.

online retailing A type of shopping available to consumers with access to the Internet.

open-ended question An interview question that encourages an answer phrased in the respondent's own words.

opinion leader An individual who influences the opinions of others.

optimizers Business customers who consider numerous suppliers, both familiar and unfamiliar, solicit bids, and study all proposals carefully before selecting one.

order fulfillment process A supply chain management process that involves generating, filling, delivering, and providing on-the-spot service for customer orders.

order processing system A system whereby orders are entered into the supply chain and filled.

order-to-cash cycle The amount of time between order placement, receipt of the customer's payment, and order shipment.

original equipment manufacturers (OEMs) Individuals and organizations that buy business goods and incorporate them into the products that they produce for eventual sale to other producers or to consumers.

outsourcing (contract logistics) A manufacturer's or supplier's use of an independent third party to manage an entire function of the logistics system, such as transportation, warehousing, or order processing.

P

penetration pricing A pricing policy whereby a firm charges a relatively low price for a product initially as a way to reach the mass market.

perception The process by which people select, organize, and interpret stimuli into a meaningful and coherent picture.

perceptual mapping A means of displaying or graphing, in two or more dimensions, the location of products, brands, or groups of products in customers' minds.

perishability The inability of services to be stored, warehoused, or inventoried.

personal selling A purchase situation involving a personal, paid-for communication between two people in an attempt to influence each other.

personality A way of organizing and grouping the consistencies of an individual's reactions to situations.

persuasive labeling A type of package labeling that focuses on a promotional theme or logo with consumer information being secondary.

pioneering advertising A form of advertising designed to stimulate primary demand for a new product or product category.

planned obsolescence The practice of modifying products so those that have already been sold become obsolete before they actually need replacement.

planning The process of anticipating future events and determining strategies to achieve organizational objectives in the future.

PLC See *product life cycle*.

point-of-purchase display A promotional display set up at the retailer's location to build traffic, advertise the product, or induce impulse buying.

point-of-sale interactions Communications between customers and organizations that occur at the point of sale, normally in a store.

pop-up shops Temporary retail establishments that provide flexible locations without a long-term commitment.

portfolio matrix A tool for allocating resources among products or strategic business units on the basis of relative market share and market growth rate.

position The place a product, brand, or group of products occupies in consumers' minds relative to competing offerings.

positioning Developing a specific marketing mix to influence potential customers' overall perception of a brand, product line, or organization in general.

postponement The delay in final production in the Leagile supply chain management strategy that enables the company to take advantage of many of the benefits of lean supply chain management while still providing the agility that improves customer experiences.

preapproach A process that describes the "homework" that must be done by a salesperson before he or she contacts a prospect.

predatory pricing The practice of charging a very low price for a product with the intent of driving competitors out of business or out of a market.

predictive modeling A data manipulation technique in which marketers try to determine, based on some past set of occurrences, what the odds are that some other occurrence, such as a response or purchase, will take place in the future.

premium An extra item offered to the consumer, usually in exchange for some proof of purchase of the promoted product.

prestige pricing Charging a high price to help promote a high-quality image.

price That which is given up in an exchange to acquire a good or service.

price bundling Marketing two or more products in a single package for a special price.

price equilibrium The price at which demand and supply are equal.

price fixing An agreement between two or more firms on the price they will charge for a product.

price lining The practice of offering a product line with several items at specific price points.

price shading The use of discounts by salespeople to increase demand for one or more products in a line.

price skimming A pricing policy whereby a firm charges a high introductory price, often coupled with heavy promotion. Over time, the price is often lowered as competition enters the marketplace.

price strategy A basic, long-term pricing framework, which establishes the initial price for a product and the intended direction for price movements over the product life cycle.

primary data Information that is collected for the first time; used for solving the particular problem under investigation.

primary membership group A reference group with which people interact regularly in an informal, face-to-face manner, such as family, friends, or fellow employees.

private brand A brand name owned by a wholesaler or a retailer.

probability sample A sample in which every element in the population has a known statistical likelihood of being selected.

problem child (question mark) In the portfolio matrix, a business unit that shows rapid growth but poor profit margins.

processed materials Products used directly in manufacturing other products.

product Everything, both favorable and unfavorable, that a person receives in an exchange.

product advertising A form of advertising that touts the benefits of a specific good or service.

product category All brands that satisfy a particular type of need.

product development A marketing strategy that entails the creation of new products for current customers.

product development A marketing strategy that entails the creation of marketable new products; the process of converting applications for new technologies into marketable products.

product development and commercialization process The group of activities that facilitates the joint development and marketing of new offerings among a group of supply chain partner firms.

product differentiation A positioning strategy that some firms use to distinguish their products from those of competitors.

product item A specific version of a product that can be designated as a distinct offering among an organization's products.

product life cycle (PLC) A biological metaphor that traces the stages of a product's acceptance, from its introduction (birth) to its decline (death).

product line A group of closely related product items.

product line depth The number of product items in a product line.

product line extension Adding additional products to an existing product line in order to compete more broadly in the industry.

product line pricing Setting prices for an entire line of products.

product mix All products that an organization sells.

product mix width The number of product lines an organization offers.

product modification Changing one or more of a product's characteristics.

product offering The mix of products offered to the consumer by the retailer; also called the product assortment or merchandise mix.

product placement A public relations strategy that involves getting a product, service, or company name to appear in a movie, television show, radio program, magazine, newspaper, video game, video or audio clip, book, or commercial for another product; on the Internet; or at special events.

product/service differentiation competitive advantage The provision of something that is unique and valuable to buyers beyond simply offering a lower price than the competition's.

production orientation A philosophy that focuses on the internal capabilities of the firm rather than on the desires and needs of the marketplace.

profit Revenue minus expenses.

profit maximization A method of setting prices that occurs when marginal revenue equals marginal cost.

promotion Communication by marketers that informs, persuades, and reminds potential buyers of a product in order to influence an opinion or elicit a response.

promotional allowance (trade allowance) A payment to a dealer for promoting the manufacturer's products.

promotional mix The combination of promotional tools—including advertising, public relations, personal selling, and sales promotion—used to reach the target market and fulfill the organization's overall goals.

promotional strategy A plan for the optimal use of the elements of promotion: advertising, public relations, personal selling, and sales promotion.

prospecting See *lead generation*.

PSA See *public service advertisement*.

psychographic segmentation Market segmentation on the basis of personality, motives, lifestyles, and geodemographics.

psychological pricing See *odd-even pricing*.

public relations The marketing function that evaluates public attitudes, identifies areas within the organization the public may be interested in, and executes a program of action to earn public understanding and acceptance.

public service advertisement (PSA) An announcement that promotes a program of a federal, state, or local government or of a nonprofit organization.

publicity Public information about a company, product, service, or issue appearing in the mass media as a news item.

pull strategy A marketing strategy that stimulates consumer demand to obtain product distribution.

pulsing media schedule A media scheduling strategy that uses continuous scheduling throughout the year coupled with a flighted schedule during the best sales periods.

purchasing power A comparison of income versus the relative cost of a set standard of goods and services in different geographic areas.

push money Money offered to channel intermediaries to encourage them to "push" products—that is, to encourage other members of the channel to sell the products.

push strategy A marketing strategy that uses aggressive personal selling and trade advertising to convince a wholesaler or a retailer to carry and sell particular merchandise.

pyramid of corporate social responsibility A model that suggests corporate social responsibility is composed of economic, legal, ethical, and philanthropic responsibilities and that the firm's economic performance supports the entire structure.

Q

quantity discount A price reduction offered to buyers buying in multiple units or above a specified dollar amount.

question mark See *problem child*.

quota A statement of the individual salesperson's sales objectives, usually based on sales volume alone but sometimes including key accounts (those with greatest potential), new accounts, repeat sales, and specific products.

R

radio-frequency identification (RFID) An automatic identification method that uses radio signals that work with scanned bar codes to identify products; data is stored in and retrieved from the RFID tag, which is attached to a product.

random error An error that occurs when the selected sample is an imperfect representation of the overall population.

random sample A sample arranged in such a way that every element of the population has an equal chance of being selected as part of the sample.

raw materials Unprocessed extractive or agricultural products, such as mineral ore, timber, wheat, corn, fruits, vegetables, and fish.

reach The number of target consumers exposed to a commercial at least once during a specific period, usually four weeks.

real self-image The way an individual actually perceives himself or herself.

rebate A cash refund given for the purchase of a product during a specific period.

receiver The person who decodes a message.

recession A period of economic activity characterized by negative growth, which reduces demand for goods and services.

reciprocity The practice of business purchasers choosing to buy from their own customers.

recruited Internet sample A sample in which respondents are prerecruited and must qualify to participate. They are then e-mailed a questionnaire or directed to a secure Web site.

reference group A group in society that influences an individual's purchasing behavior.

referral A recommendation to a salesperson from a customer or business associate.

reintermediation The reintroduction of an intermediary between producers and users.

relationship commitment A firm's belief that an ongoing relationship with another firm is so important that the relationship warrants maximum efforts at maintaining it indefinitely.

relationship integration The ability of two or more companies to develop social connections that serve to guide their interactions when working together.

relationship marketing A strategy that focuses on keeping and improving relationships with current customers.

relationship selling (consultative selling) A sales practice that involves building, maintaining, and enhancing interactions with customers in order to develop long-term satisfaction through mutually beneficial partnerships.

reliability The ability to perform a service dependably, accurately, and consistently.

repositioning Changing consumers' perceptions of a brand in relation to competing brands.

resale price maintenance A manufacturer, and its distributors,

agree that retailers will sell products at a certain price floor.
research design Specifies which research questions must be answered, how and when the data will be gathered, and how the data will be analyzed.
response list A customer list that includes the names and addresses of individuals who have responded to an offer of some kind, such as by mail, telephone, direct-response television, product rebates, contests or sweepstakes, or billing inserts.
responsiveness The ability to provide prompt service.
retailer A channel intermediary that sells mainly to consumers.
retailing All the activities directly related to the sale of goods and services to the ultimate consumer for personal, nonbusiness use.
retailing mix A combination of the six Ps—product, place, promotion, price, presentation, and personnel—to sell goods and services to the ultimate consumer.
return on investment (ROI) Net profit after taxes divided by total assets.
returns management process A process that enables firms to manage volumes of returned product efficiently, while minimizing costs and maximizing the value of the returned assets to the firms in the supply chain.
revenue The price charged to customers multiplied by the number of units sold.
RFID See *radio-frequency identification.*
role specificity When each firm in a supply chain has clarity in terms of knowing which firm is the leader, which firms are the followers, and which responsibilities are assigned to each firm.
routine response behavior The type of decision making exhibited by consumers buying frequently purchased, low-cost goods and services; requires little search and decision time.

S

sales cycle See *sales process.*
sales orientation The idea that people will buy more goods and services if aggressive sales techniques are used and that high sales result in high profits.
sales presentation A formal meeting in which the salesperson presents a sales proposal to a prospective buyer.
sales process (sales cycle) The set of steps a salesperson goes through in a particular organization to sell a particular product or service.
sales promotion Marketing activities—other than personal selling, advertising, and public relations—that stimulate consumer buying and dealer effectiveness.
sales proposal A formal written document or professional presentation that outlines how the salesperson's product or service will meet or exceed the prospect's needs.
sample A subset from a larger population.
sampling A promotional program that allows the consumer the opportunity to try a product or service for free.
sampling error An error that occurs when a sample somehow does not represent the target population.
satisficers Business customers who place an order with the first familiar supplier to satisfy product and delivery requirements.
SBU See *strategic business unit.*
scaled-response question A closed-ended question designed to measure the intensity of a respondent's answer.
scanner-based research A system for gathering information from a single group of respondents by continuously monitoring the advertising, promotion, and pricing they are exposed to and the things they buy.
scrambled merchandising The tendency to offer a wide variety of nontraditional goods and services under one roof.
screened Internet sample An Internet sample with quotas based on desired sample characteristics.
screening The first filter in the product development process, which eliminates ideas that are inconsistent with the organization's new-product strategy or are obviously inappropriate for some other reason.
search quality A characteristic that can be easily assessed before purchase.
seasonal discount A price reduction for buying merchandise out of season.
seasonal media schedule A media scheduling strategy that runs advertising only during times of the year when the product is most likely to be used.
secondary data Data previously collected for any purpose other than the one at hand.
secondary membership group A reference group with which people associate less consistently and more formally than a primary membership group, such as a club, professional group, or religious group.
segmentation bases (variables) Characteristics of individuals, groups, or organizations.
selective distortion A process whereby a consumer changes or distorts information that conflicts with his or her feelings or beliefs.
selective distribution A form of distribution achieved by screening dealers to eliminate all but a few in any single area.
selective exposure The process whereby a consumer notices certain stimuli and ignores others.
selective retention A process whereby a consumer remembers only that information that supports his or her personal beliefs.
self-concept How consumers perceive themselves in terms of attitudes, perceptions, beliefs, and self-evaluations.
selling against the brand Stocking well-known branded items at high prices in order to sell store brands at discounted prices.
sender The originator of the message in the communication process.
service mark A trademark for a service.
service The result of applying human or mechanical efforts to people or objects.
shopping product A product that requires comparison shopping because it is usually more expensive than a convenience product and is found in fewer stores.
simulated (laboratory) market testing The presentation of advertising and other promotion materials for several products, including a test product, to members of the product's target market.
simultaneous product development A team-oriented approach to new-product development.
single-price tactic A price tactic that offers all goods and services at the same price (or perhaps two or three prices).
site reach See *stickiness.*
social class A group of people in a society who are considered nearly equal in status or community esteem, who regularly socialize among themselves both formally and informally, and who share behavioral norms.

GLOSSARY

socialization process How cultural values and norms are passed down to children.

societal marketing orientation The idea that an organization exists not only to satisfy customer wants and needs and to meet organizational objectives, but also to preserve or enhance individuals' and society's long-term best interests.

spatial discrepancy The difference between the location of a producer and the location of widely scattered markets.

specialty discount store A retail store that offers a nearly complete selection of single-line merchandise and uses self-service, discount prices, high volume, and high turnover.

specialty product A particular item for which consumers search extensively and are very reluctant to accept substitutes.

specialty store A retail store specializing in a given type of merchandise.

sponsorship A public relations strategy in which a company spends money to support an issue, cause, or event that is consistent with corporate objectives, such as improving brand awareness or enhancing corporate image.

stakeholder theory A theory that holds that social responsibility is paying attention to the interest of every affected stakeholder in every aspect of a firm's operation.

star In the portfolio matrix, a business unit that is a fast-growing market leader.

status quo pricing A pricing objective that maintains existing prices or meets the competition's prices.

stickiness (site reach) A measure of a Web site's effectiveness; calculated by multiplying the frequency of visits times the duration of a visit times the number of pages viewed during each visit.

stimulus Any unit of input affecting one or more of the five senses: sight, smell, taste, touch, hearing.

stimulus discrimination A learned ability to differentiate among similar products.

stimulus generalization A form of learning that occurs when one response is extended to a second stimulus similar to the first.

straight rebuy A situation in which the purchaser reorders the same goods or services without looking for new information or investigating other suppliers.

strategic alliance (strategic partnership) A cooperative agreement between business firms.

strategic business unit (SBU) A subgroup of a single business or a collection of related businesses within the larger organization.

strategic channel alliance A cooperative agreement between business firms to use the other's already established distribution channel.

strategic partnership See *strategic alliance.*

strategic planning The managerial process of creating and maintaining a fit between the organization's objectives and resources and evolving market opportunities.

subculture A homogeneous group of people who share elements of the overall culture as well as unique elements of their own group.

supercenter A retail store that combines groceries and general merchandise goods with a wide range of services.

supermarket A large, departmentalized, self-service retailer that specializes in food and some nonfood items.

supplementary services A group of services that support or enhance the core service.

supplier relationship management process A supply chain management process that supports manufacturing flow by identifying and maintaining relationships with highly valued suppliers.

supplies Consumable items that do not become part of the final product.

supply The quantity of a product that will be offered to the market by suppliers at various prices for a specified period.

supply chain The connected chain of all of the business entities, both internal and external to the company, that perform or support the logistics function.

supply chain integration When multiple firms in a supply chain coordinate their activities and processes so that they are seamlessly linked to one another in an effort to satisfy the customer.

supply chain management A management system that coordinates and integrates all of the activities performed by supply chain members into a seamless process, from the source to the point of consumption, resulting in enhanced customer and economic value.

supply chain orientation The connected chain of all of the business entities, both internal and external to the company, that perform or support the logistics function.

supply chain team An entire group of individuals who orchestrate the movement of goods, services, and information from the source to the consumer.

survey research The most popular technique for gathering primary data, in which a researcher interacts with people to obtain facts, opinions, and attitudes.

sustainability The idea that socially responsible companies will outperform their peers by focusing on the world's social problems and viewing them as opportunities to build profits and help the world at the same time.

sustainable competitive advantage An advantage that can not be copied by the competition.

SWOT analysis Identifying internal strengths (S) and weaknesses (W) and also examining external opportunities (O) and threats (T).

systems approach A key principle of supply chain management—that multiple firms work together to perform tasks as a single, unified system, rather than as several individual companies acting in isolation.

T

tangibles The physical evidence of a service, including the physical facilities, tools, and equipment used to provide the service.

target market A defined group most likely to buy a firm's product.

target market A group of people or organizations for which an organization designs, implements, and maintains a marketing mix intended to meet the needs of that group, resulting in mutually satisfying exchanges.

teamwork Collaborative efforts of people to accomplish common objectives.

technology and planning integration The creation and maintenance of information technology systems that connect managers across and through the firms in the supply chain.

telemarketing The use of the telephone to sell directly to consumers.

temporal discrepancy A situation that occurs when a product is produced but a customer is not ready to buy it.

test marketing The limited introduction of a product and a marketing program to determine the reactions of potential customers in a market situation.
third-party logistics firm (3PL) A firm that is contracted to manage part or all of another firm's order fulfillment process.
touch points All possible areas of a business where customers communicate with that business.
trade allowance A price reduction offered by manufacturers to intermediaries, such as wholesalers and retailers. See *promotional allowance*.
trade discount See *functional discount*.
trade sales promotion Sales promotion activities targeting a channel member, such as a wholesaler or retailer.
trademark The exclusive right to use a brand or part of a brand.
trust The condition that exists when one party has confidence in an exchange partner's reliability and integrity.
two-part pricing A price tactic that charges two separate amounts to consume a single good or service.

U

unbundling Reducing the bundle of services that comes with the basic product.
undifferentiated targeting strategy A marketing approach that views the market as one big market with no individual segments and thus uses a single marketing mix.
unfair trade practice acts Laws that prohibit wholesalers and retailers from selling below cost.
uniform delivered pricing A price tactic in which the seller pays the actual freight charges and bills every purchaser an identical, flat freight charge.
unique selling proposition A desirable, exclusive, and believable advertising appeal selected as the theme for a campaign.
unitary elasticity A situation in which total revenue remains the same when prices change.
universal product codes (UPCs) A series of thick and thin vertical lines (bar codes), readable by computerized optical scanners, that represent numbers used to track products.
universe The population from which a sample will be drawn.
unsought product A product unknown to the potential buyer, or a known product that the buyer does not actively seek.
UPCs See *universal product codes*.
Uruguay Round An agreement to dramatically lower trade barriers worldwide; created the World Trade Organization.
usage-rate segmentation Dividing a market by the amount of product bought or consumed.
utilitarian ethical theory A theory that holds that the choice that yields the greatest benefit to the most people is the choice that is ethically correct.

V

value The enduring belief that a specific mode of conduct is personally or socially preferable to another mode of conduct.
value-based pricing Setting the price at a level that seems to the customer to be a good price compared to the prices of other options.
variable cost A cost that varies with changes in the level of output.
variable pricing See *flexible pricing*.
variables See *segmentation bases*.
vertical conflict A channel conflict that occurs between different levels in a marketing channel, most typically between the manufacturer and wholesaler or between the manufacturer and retailer.
vertical structure One of three dimensions of supply chain network design; the number of suppliers or customers included within each individual tier.
virtue A character trait valued as being good.

W

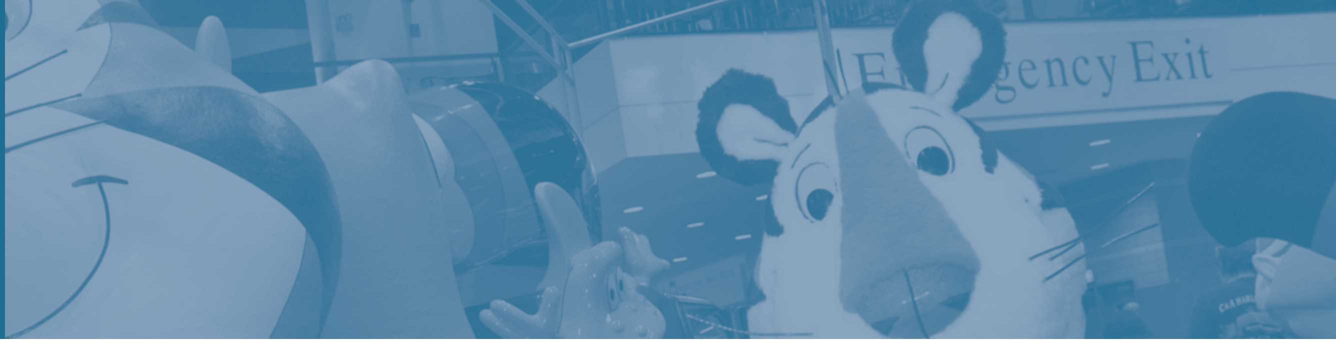
want Recognition of an unfulfilled need and a product that will satisfy it.
warehouse membership clubs Limited-service merchant wholesalers that sell a limited selection of brand-name appliances, household items, and groceries on a cash-and-carry basis to members, usually small businesses and groups.
warranty A confirmation of the quality or performance of a good or service.
World Bank An international bank that offers low-interest loans, advice, and information to developing nations.
World Trade Organization (WTO) A trade organization that replaced the old General Agreement on Tariffs and Trade (GATT).
WTO See *World Trade Organization*.

Y

yield management systems (YMS) A technique for adjusting prices that uses complex mathematical software to profitably fill unused capacity by discounting early purchases, limiting early sales at these discounted prices, and overbooking capacity.
YMS See *yield management systems*.

Z

zone pricing A modification of uniform delivered pricing that divides the United States (or the total market) into segments or zones and charges a flat freight rate to all customers in a given zone.



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MARKETING PLAN APPENDIX

The authors would like to thank e-motion software for allowing us to include its marketing plan in the Tenth Edition of Marketing. We greatly appreciate Mr. Keohane's contribution of a real plan used by his growing company, which demonstrates to students the level of detail and the elements required to build an effective plan.

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ORGANIZATIONAL INDEX

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SUBJECT INDEX

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ANATOMY OF A Multinational Company

Starbucks

Starbucks has coffee shops in 27 different countries.

Strategic Fit

Starbucks chooses locations with shared values and strategic fit.

Australia, Austria, Beijing, Brazil, Canada, China, Czech Republic, France, Germany, Greece, Hawaii, Hong Kong, Ireland, Japan, Malaysia, Mexico, New Zealand, Peru, Shanghai, Singapore, South Korea, Spain, Switzerland, Taiwan, Thailand, Turkey, United Kingdom

(AP Photo/Moises Castillo)

Local Culture

Adapting to local culture helps maintain global business.

Familiar logo

Familiar logo ensures global marketing standardization.

Customer Experience

Starbucks maintains control of its customer experience through joint ventures and company-owned operations.

That's Marketing!

NEW! "Anatomy of" Feature

Each part in the Tenth Edition of *Marketing* now includes a unique new graphic that vividly illustrates a particular part concept. Each "Anatomy of" is set on a full page and uses exceptional photography to show how the elements of a concept connect. Highlighting a multinational company, the buying decision, packaging design, product life cycle, store layout, integrated marketing campaign, and more, these "Anatomies" help you visualize the connection between marketing concepts and your real-world application.

"Anatomy of" features are integrated throughout the book:

Part 1—Chapter 5: Developing a Global Vision
Anatomy of a Multinational Company • Starbucks

Part 2—Chapter 6: Consumer Decision Making
Anatomy of a Buying Decision • Car

Part 3—Chapter 10: Product Concepts
Anatomy of a Packaging Decision • Barbie

Chapter 11: Developing and Managing Products
Anatomy of a Product Life Cycle • VCRs

Part 4—Chapter 13: Marketing Channels
Anatomy of a Marketing Channel • Electronics

Chapter 15: Retailing
Anatomy of a Store Layout • Grocery

Part 5—Chapter 16: Promotional Planning for Competitive Advantage
Anatomy of an Integrated Marketing Campaign • Indiana Jones movie

Chapter 17: Advertising and Public Relations
Anatomy of an Ad • Yoplait

Part 6—Chapter 20: Setting the Right Price
Anatomy of Product Line Pricing • McDonald's

Part 7—Chapter 21: Customer Relationship Management
Anatomy of a Customer Relations Decision • Sports team