

CHAPTER 2

REVIEW OF LITERATURE

This chapter reviews the literature relevant to distribution channels.

2.1 Intermediate and Industrial products

Steel bars and cement are intermediate products. These are used to produce other products or services. It can be classified according to the extent to which they enter the production process (Ballou 1978), i.e.,

- a) Goods that are part of the finished products such as raw materials and component parts.
- b) Goods that are used in the manufacturing process such as buildings and equipment.
- c) Goods that do not enter the process directly such as supplies and business services.

The cement and steel bars are under category (a). However, such industrial product classification may not be as useful for logistical-planning purposes as for consumer-products classification (Ballou 1978).

2.2 The Need for Distribution Channels

A distribution channel is a set of interdependent organisations involved in the process of making a product or service available for use or consumption by the consumer or industrial user (Stern and El-Ansary 1988). Most manufacturers use middlemen who bring their products to end users. This means losing control over how or to whom the products are sold. However, there are many advantages from using middlemen.

Many producers lack the financial resources to carry out direct marketing. Direct marketing will require many producers to become middlemen for the products of other producers in order to achieve mass distribution economies. Even if producers have the financial resources, producers can often earn a greater return by concentrating on their main business.

Producers make assortments of products in large quantities whereas consumers want broad assortments of products in small quantities. Middlemen could buy

large quantities of many products and break them down into smaller quantities and broader assortments wanted by consumers. In addition, middlemen help bridge the communication and information gap. Consumers normally do not know the productive sources of the goods they want and manufacturers do not know who and where are the potential purchasers of their products. Therefore, middlemen play an important matching role of supply and demand.

2.3 Functions of Distribution Channels

Members of the distribution channels perform many key functions (Kotler and Armstrong 1991). These are provision of information, promotion, contact, matching, negotiation, physical distribution, financing and risk taking.

Provision of information refers to gathering and distributing information in the marketing environment needed for planning. Promotion involves developing and spreading persuasive communications about an offer. Contact means finding and communicating with prospective buyers. Matching refers to shaping and fitting the offer to the buyer's needs, including such activities as manufacturing, grading, assembling and packaging. Negotiation means reaching an agreement on price and other terms of the offer so that ownership or possession can be transferred. Transporting and storing goods comes under physical distribution. Financing refers

to acquiring and using funds to cover the costs of the channel work and risk taking is to assume the risks of carrying out the channel work.

However, channels for industrial products usually do not include a middlemen than those for consumer products (Guirdham 1972). This is due to reasons such as the tailoring of manufacturer' products to purchasers' requirements, the need for after-sales maintenance and the requirement of technical or application assistance before or after sales.

These needs lead manufacturers to take responsibility for both the essential channel functions of exchange and physical distribution.

Industrial stockists or distributors commonly carry competing lines and tend to direct demand from one manufacturer to another if the original item is temporarily out of stock. Often the distributor is required to fulfill a creative marketing function and to provide a maintenance and technical or applications service. Industrial distributors ensure rapid delivery to customers; because distributors normally provide a number of lines from one source of supply. The customer may be able to save transaction costs by accumulating a number of products on one purchase order. Moreover, a small account with a manufacturer can be a large

account with the distributor thereby commanding increased customer importance and services.

Distributors in building material trade deal in a variety of materials used by builders, ranging from steel bars, cement, gravel, bricks to glazed tiles, glass, paints and other decorative products. The supplies of building materials industry are a heterogeneous collection of companies of widely different size. Their customers are contractors, decorators, developers and architects. However, most of the sales are made to contractors.

Granting credit to customers is almost universal and is regarded as an important factor not only in maintaining goodwill but ensuring survival of limited resources small contractors. Cost of credit and bad debts can sometimes wipe off accumulated profit of building materials distributors during an economic downturn. From the manufacturers' point of view, willingness of building materials distributors in granting credit and their better credit assessment of contractors in their location increases sales, while manufacturers avoid incurring bad debts and handling of uneconomical small accounts.

2.4 Number of Distribution Channel Levels

The number of distribution channel levels refers to the number of layers of middlemen that perform the work of bringing the product closer to final buyer.

The number of intermediary levels indicates the length of a channel.

In consumer markets, distribution channels with more than four levels is uncommon whereas in industrial distribution channel it is rarely more than two levels. The greater the number of levels, the less control and the more complex is the distribution channels.

2.5 Channel Design Decisions

Before channel decisions are made, manufacturers need to analyse customers service needs, set channel objectives and constraints, and identify and evaluate channel alternatives available.

To design an effective channel, manufacturer need to know the service levels desired by customers, and manufacturer must balance customer services needs against customer price preferences (Stern and Sturdivant 1986). Channel objectives are influenced by the nature of products, company policies, middlemen, competitors and environment.

Once channel objectives have been defined, manufacturers should next identify its major channel alternatives in terms of types of middlemen, number of middlemen and the responsibilities of each channel member. A firm should identify the types of middlemen available to carry on its channel works which can take the form of company salesforce, manufacturer's agency or industrial distributors.

2.6 Channel Management Decisions

Once channel alternatives have been reviewed and the best channel design decided, the manufacturer must implement and manage the chosen channel. Channel management calls for selecting and motivating individual middlemen and evaluating their performance.

In selecting channel members, the manufacturers should determine which characteristics distinguish the better middlemen. It include the middlemen's years in business, other lines carried, growth and profit record, profitability, cooperativeness, reputation, the number and character of the product lines carried and the size and quality of sales force. Others include middlemen's customers, their location and future growth potential.

Channel members require continuous motivation to do their best. Manufacturers

must sell to middlemen and not through them. Most producers see the problem as finding ways to gain middlemen's cooperation (Roosenbloom 1978). Carrot-and-stick approach is commonly used. In positive motivation, higher margins, special deals, premium, cooperative advertising allowances and sales contests are offered. At times negative motivators such as threatening to reduce margins, to slow down delivery, or to end the relationship are employed.

Middlemen's performance needs to be constantly evaluated. Performance must be checked against standards such as sales quota, average inventory levels, customer delivery time, treatment of damaged and lost goods, cooperation in company promotion and training programs, and services to customers. Manufacturers should reorganise and reward performing middlemen, and help or replaced non-performing ones.