



# Wholesaling, Retailing, and Physical Distribution

# 14

## Learning Objectives

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What you will be able to do once you complete this chapter:

- 1 Identify the various channels of distribution that are used for consumer and industrial products.
- 2 Explain the concept of market coverage.
- 3 Understand how supply-chain management facilitates partnering among channel members.
- 4 Describe what a vertical marketing system is and identify the types of vertical marketing systems.
- 5 Discuss the need for wholesalers and describe the services they provide to retailers and manufacturers.
- 6 Identify and describe the major types of wholesalers.
- 7 Distinguish among the major types of retailers.
- 8 Identify the categories of shopping centers and the factors that determine how shopping centers are classified.
- 9 Explain the five most important physical distribution activities.

**Did You Know?**

**Founded in 1996, GameStop now rings up \$9 billion in annual sales through 6,450 stores in 17 countries.**

**GameStop's Game Plan for Global Retailing**

From Dallas, Texas, to Dee Why, Australia, GameStop is a big player in video-game retailing. The company, based in Grapevine, Texas, was founded in 1996 and now rings up \$9 billion in annual sales through 6,450 stores in 17 countries. GameStop targets three customer segments: enthusiasts who want the newest or hottest consoles and games, consumers who are casual game-players, and consumers who give games or accessories as gifts. Its game plan for global success is based on an ever-changing store assortment of new and used games and game consoles.

Under GameStop's trade-in program, customers who bring in used games, consoles, or accessories can receive store credit toward the purchase of other merchandise. GameStop ships used items to one of its three refurbishment centers to be tested, fixed if necessary, repackaged, and sent back to the stores for resale. This trade-in program stimulates a steady stream of store traffic and adds to GameStop's inventory. Just as important, it boosts GameStop's profitability, because gross margins on sales of used merchandise are much higher than on sales of new merchandise. In fact, 25 percent of GameStop's revenue and 45 percent of its profits now come from retailing used games.

Thanks to its sophisticated information system, GameStop knows exactly which items are in demand in each location. Analyzing what sells where (and how quickly) also helps the company allocate supplies of new games and consoles. To ensure that new products reach store shelves as quickly as possible, GameStop has one distribution center devoted to handling new items and a second distribution center that handles all other merchandise. The company monitors daily sales in each store and automatically ships replenishment stock twice a week, freeing store staff to concentrate on serving customers.

GameStop has been building up its online presence to cater to consumers who prefer to buy with a click. Its Web site provides previews of soon-to-be-released games, invites customers to pre-order new games, and offers downloads of new and classic games, some for sale and some for free. Although digital downloads are increasingly popular, GameStop believes that its in-store retailing strength will keep the company ahead of the game for years to come.<sup>1</sup>

**S**ome companies, like GameStop, use a particular approach to distribution and marketing channels that gives them a sustainable competitive advantage. More than 2 million firms in the United States help to move products from producers to consumers. Store chains such as Dollar General Stores, Starbucks, Sears, and Walmart operate retail outlets where consumers make purchases. Some retailers, such as Avon Products and Amway, send their salespeople to the homes of customers. Other retailers, such as Lands' End and L.L.Bean, sell through both catalogs and online. Still others, such as Amazon, sell online to customers.

In addition, there are more than half a million wholesalers that sell merchandise to other firms. Most consumers know little about these firms, which work "behind the scenes" and rarely sell directly to consumers. These and other intermediaries are concerned with the transfer of both products and ownership. They thus help to create the time, place, and possession utilities that are critical to marketing. As we will see, they also perform a number of services for their suppliers and their customers.

In this chapter, we initially examine various channels of distribution that products follow as they move from producer to ultimate user. Then we discuss wholesalers and retailers within these channels. Next, we examine the types of shopping centers. Finally, we explore the physical distribution function and the major modes of transportation that are used to move goods.

## Channels of Distribution

A **channel of distribution**, or **marketing channel**, is a sequence of marketing organizations that directs a product from the producer to the ultimate user. Every marketing channel begins with the producer and ends with either the consumer or the business user.

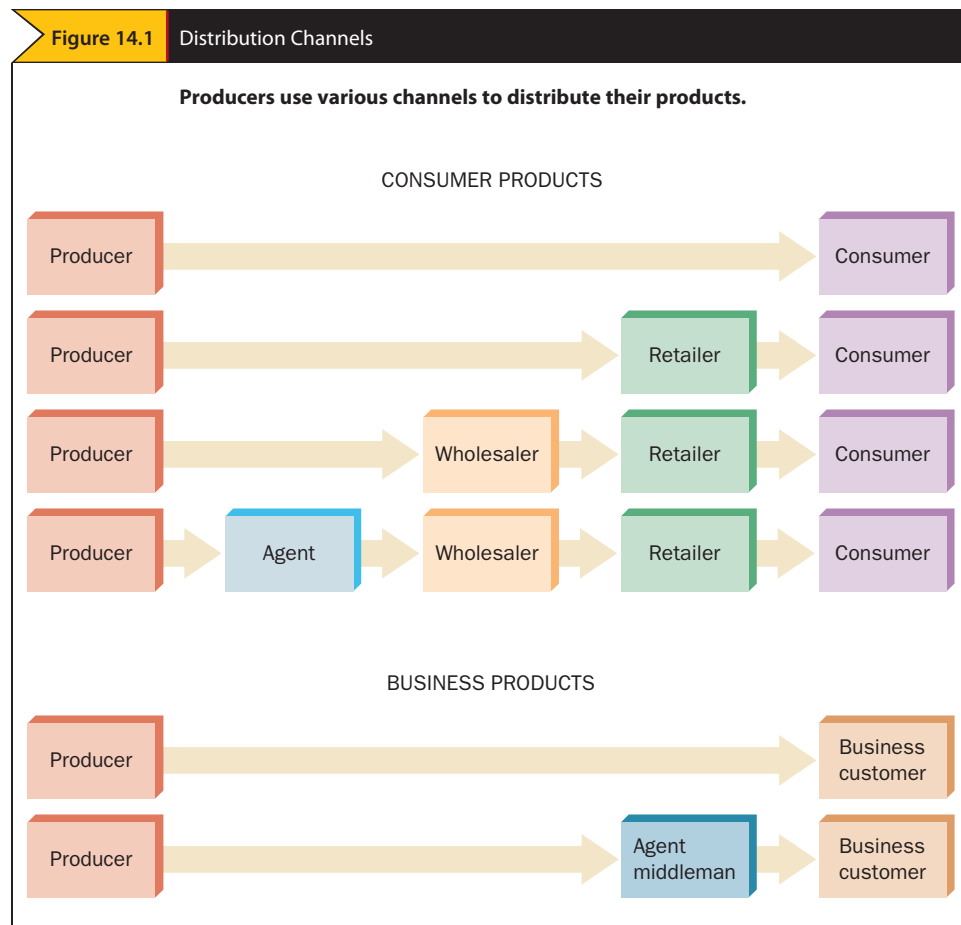
A marketing organization that links a producer and user within a marketing channel is called a **middleman** or **marketing intermediary**. For the most part, middlemen are concerned with the transfer of *ownership* of products. A **merchant middleman** (or, more simply, a *merchant*) is a middleman that actually takes title to products by buying them. A **functional middleman**, on the other hand, helps in the transfer of ownership of products but does not take title to the products.

## Channels for Consumer Products

Different channels of distribution generally are used to move consumer and business products. The four most commonly used channels for consumer products are illustrated in Figure 14.1.

**Producer to Consumer** This channel, often called the *direct channel*, includes no marketing intermediaries. Practically all services and a few consumer goods are distributed through a direct channel. Examples of marketers that sell goods directly to consumers include Dell Computer, Mary Kay Cosmetics, and Avon Products.

Producers sell directly to consumers for several reasons. They can better control the quality and price of their products. They do not have to pay (through discounts) for the services of intermediaries. They can maintain closer ties with customers.



Identify the various channels of distribution that are used for consumer and industrial products.

**channel of distribution (or marketing channel)** a sequence of marketing organizations that directs a product from the producer to the ultimate user

**middleman (or marketing intermediary)** a marketing organization that links a producer and user within a marketing channel

**merchant middleman** a middleman that actually takes title to products by buying them

**functional middleman** a middleman that helps in the transfer of ownership of products but does not take title to the products



**Marketing channels for consumer products.** Clothing like Levi's products is often distributed through the producer-retailer consumer channel.

**Producer to Retailer to Consumer** A **retailer** is a middleman that buys from producers or other middlemen and sells to consumers. Producers sell directly to retailers when retailers (such as Walmart) can buy in large quantities. This channel is used most often for products that are bulky, such as furniture and automobiles, for which additional handling would increase selling costs. It is also the usual channel for perishable products, such as fruits and vegetables, and for high-fashion products that must reach the consumer in the shortest possible time.

### **Producer to Wholesaler to Retailer to Consumer**

This channel is known as the *traditional channel* because many consumer goods (especially convenience goods) pass through wholesalers to retailers. A **wholesaler** is a middleman that sells products to other firms. These firms may be retailers, industrial users, or other wholesalers. A producer uses wholesalers when its products are carried

by so many retailers that the producer cannot deal with all of them. For example, the maker of Wrigley's gum uses this type of channel.

### **Producer to Agent to Wholesaler to Retailer to Consumer**

Producers may use agents to reach wholesalers. Agents are functional middlemen who do not take title to products and are compensated by commissions paid by producers. Often these products are inexpensive, frequently purchased items. For example, to reach a large number of potential customers, a small manufacturer of gas-powered lawn edgers might choose to use agents to market its product to wholesalers, which, in turn, sell the lawn edgers to a large number of retailers. This channel is also used for highly seasonal products (such as Christmas tree ornaments) and by producers that do not have their own sales forces.

## **Multiple Channels for Consumer Products**

Often, a manufacturer uses different distribution channels to reach different market segments. A manufacturer uses multiple channels, for example, when the same product is sold to consumers and business customers. Multiple channels are also used to increase sales or to capture a larger share of the market. With the goal of selling as much merchandise as possible, Firestone markets its tires through its own retail outlets as well as through independent dealers.

## **Channels for Business Products**

Producers of business products generally tend to use short channels. We will outline the two that are used most commonly, which are illustrated in Figure 14.1.

**Producer to Business User** In this direct channel, the manufacturer's own sales force sells directly to business users. Heavy machinery, airplanes, and major equipment usually are distributed in this way. The very short channel allows the producer to provide customers with expert and timely services, such as delivery, machinery installation, and repairs.

**Producer to Agent Middleman to Business User** Manufacturers use this channel to distribute such items as operating supplies, accessory equipment, small tools, and standardized parts. The agent is an independent intermediary between the producer and the user. Generally, agents represent sellers.

**retailer** a middleman that buys from producers or other middlemen and sells to consumers

**wholesaler** a middleman that sells products to other firms

© AP Images/PRNewsFoto/The Levi's brand

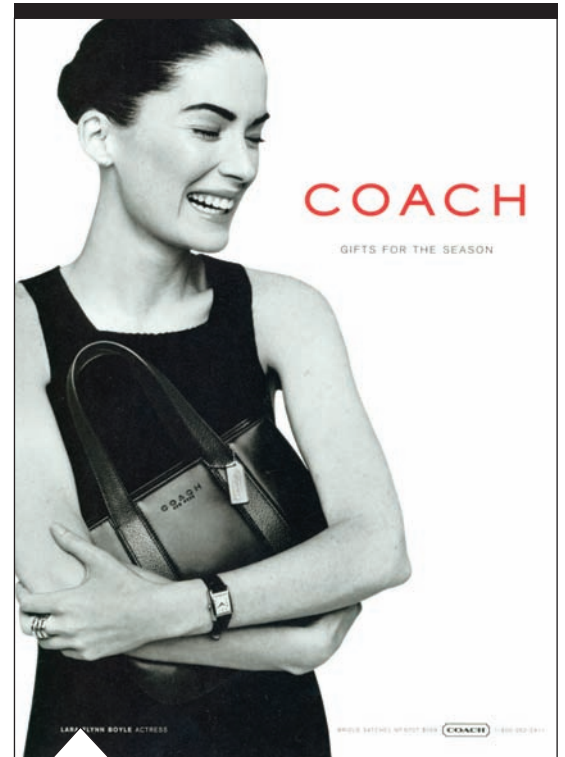
## Level of Market Coverage

The level of market coverage refers to the number of wholesalers and the number of retailers that are used for a specific geographic area. There are three levels of market coverage: intensive distribution, selective distribution, and exclusive distribution. Figure 14.2 shows examples of products that are likely to be distributed through each of these levels of market coverage.

**Intensive distribution** is the use of all available outlets for a product. The producer that wants to give its product the widest possible exposure in the marketplace chooses intensive distribution. The manufacturer saturates the market by selling to any intermediary of good financial standing that is willing to stock and sell the product. For the consumer, intensive distribution means being able to shop at a convenient store and spend a minimum amount of time buying the product. Companies such as Procter & Gamble that produce consumer packaged items rely on intensive distribution for many of their products because consumers want ready availability.

**Selective distribution** is the use of only a portion of the available outlets for a product in each geographic area. Examples include the launch of Apple's iPhone, distributed in AT&T and Apple retail stores in the United States, and perfumes distributed through large department and specialty perfume stores. The majority of perfumes and colognes use selective distribution to maintain a particular image. For example, eBay was recently fined by a Parisian court for selling certain brands of perfume on its Web site, such as Christian Dior, Givenchy, and Kenzo. These companies are trying to protect their brand's image by only selling through select retail outlets.<sup>2</sup>

Explain the concept of market coverage.



**Selective distribution.** Coach brand products are distributed through selective distribution.

Figure 14.2 Levels of Market Coverage



Image courtesy of The Advertising Archives

Source: William M. Pride and O. C. Ferrell, *Foundations of Marketing* (Mason, OH: South-Western/Cengage Learning, 2011), 319.

**intensive distribution** the use of all available outlets for a product  
**selective distribution** the use of only a portion of the available outlets for a product in each geographic area

### 3

Understand how supply-chain management facilitates partnering among channel members.

**exclusive distribution** the use of only a single retail outlet for a product in a large geographic area

**supply-chain management** long-term partnership among channel members working together to create a distribution system that reduces inefficiencies, costs, and redundancies while creating a competitive advantage and satisfying customers

**vertical channel integration** the combining of two or more stages of a distribution channel under a single firm's management

### 4

Describe what a vertical marketing system is and identify the types of vertical marketing systems.

**vertical marketing system (VMS)** a centrally managed distribution channel resulting from vertical channel integration

**Exclusive distribution** is the use of only a single retail outlet for a product in a large geographic area. Exclusive distribution usually is limited to very prestigious products. The producer usually places many requirements (such as inventory levels, sales training, service quality, and warranty procedures) on exclusive dealers. For example, Patek Philippe watches, which may sell for \$10,000 or more, are available in only a few select locations.

## Partnering Through Supply-Chain Management

**Supply-chain management** is a long-term partnership among channel members working together to create a distribution system that reduces inefficiencies, costs, and redundancies while creating a competitive advantage and satisfying customers. Supply-chain management requires cooperation throughout the entire marketing channel, including manufacturing, research, sales, advertising, and shipping. Supply chains focus not only on producers, wholesalers, retailers, and customers but also on component-parts suppliers, shipping companies, communication companies, and other organizations that participate in product distribution. Suppliers are having a greater impact on determining what items retail stores carry. This phenomenon, called *category management*, is becoming common for mass merchandisers, supermarkets, and convenience stores. Through category management, the retailer asks a supplier in a particular category how to stock the shelves. Many retailers and suppliers claim this process delivers maximum efficiency.

Traditionally, buyers and sellers have been adversarial when negotiating purchases. Supply-chain management, however, encourages cooperation in reducing the costs of inventory, transportation, administration, and handling; in speeding order-cycle times; and in increasing profits for all channel members. When buyers, sellers, marketing intermediaries, and facilitating agencies work together, customers' needs regarding delivery, scheduling, packaging, and other requirements are better met. Home Depot, North America's largest home-improvement retailer, is working to help its suppliers improve productivity and thereby supply Home Depot with better-quality products at lower costs. The company has even suggested a cooperative partnership with its competitors so that regional trucking companies making deliveries to all these organizations can provide faster, more efficient delivery.

Technology has enhanced the implementation of supply-chain management significantly. Through computerized integrated information sharing, channel members reduce costs and improve customer service. At Walmart, for example, supply-chain management has almost eliminated the occurrence of out-of-stock items. Using barcode and electronic data interchange (EDI) technology, stores, warehouses, and suppliers communicate quickly and easily to keep Walmart's shelves stocked with items customers want. Furthermore, there are currently about 400 electronic trading communities made up of businesses selling to other businesses, including auctions, exchanges, e-procurement hubs, and multi-supplier online catalogs. As many major industries transform their processes over the next five to ten years, the end result will be increased productivity by reducing inventory, shortening cycle time, and removing wasted human effort.

## Vertical Marketing Systems

**Vertical channel integration** occurs when two or more stages of a distribution channel are combined and managed by one firm. A **vertical marketing system (VMS)** is a centrally managed distribution channel resulting from vertical channel integration. This merging eliminates the need for certain intermediaries. One member of a marketing channel may assume the responsibilities of another member, or it actually may purchase the operations of that member. PepsiCo, for example, recently purchased PepsiAmericas and The Pepsi Bottling Group, both of which own and operate local bottling and distribution organizations. Although the purchase may trigger antitrust concerns, it represents a new strategy among beverage manufacturers to better control the distribution and marketing of all of their drink products, not just

sodas, as consumers increasingly buy other beverages, such as energy drinks, juices, and flavored waters.<sup>3</sup> Total vertical integration occurs when a single management controls all operations from production to final sale. Oil companies that own wells, transportation facilities, refineries, terminals, and service stations exemplify total vertical integration.

There are three types of VMSs: administered, contractual, and corporate. In an *administered VMS*, one of the channel members dominates the other members, perhaps because of its large size. Under its influence, the channel members collaborate on production and distribution. A powerful manufacturer, such as Procter & Gamble, receives a great deal of cooperation from intermediaries that carry its brands. Although the goals of the entire system are considered when decisions are made, control rests with individual channel members, as in conventional marketing channels. Under a *contractual VMS*, cooperative arrangements and the rights and obligations of channel members are defined by contracts or other legal measures. In a *corporate VMS*, actual ownership is the vehicle by which production and distribution are joined. For example, The Limited established a corporate VMS that operates corporate-owned production facilities and retail stores. Most VMSs are organized to improve distribution by combining individual operations.

5

## Marketing Intermediaries: Wholesalers

Wholesalers may be the most misunderstood of marketing intermediaries. Producers sometimes try to eliminate them from distribution channels by dealing directly with retailers or consumers. Yet wholesalers provide a variety of essential marketing services. Although wholesalers can be eliminated, their functions cannot be eliminated. These functions *must* be performed by other channel members or by consumers. Eliminating a wholesaler may or may not cut distribution costs.

Discuss the need for wholesalers and describe the services they provide to retailers and manufacturers.

### Justifications for Marketing Intermediaries

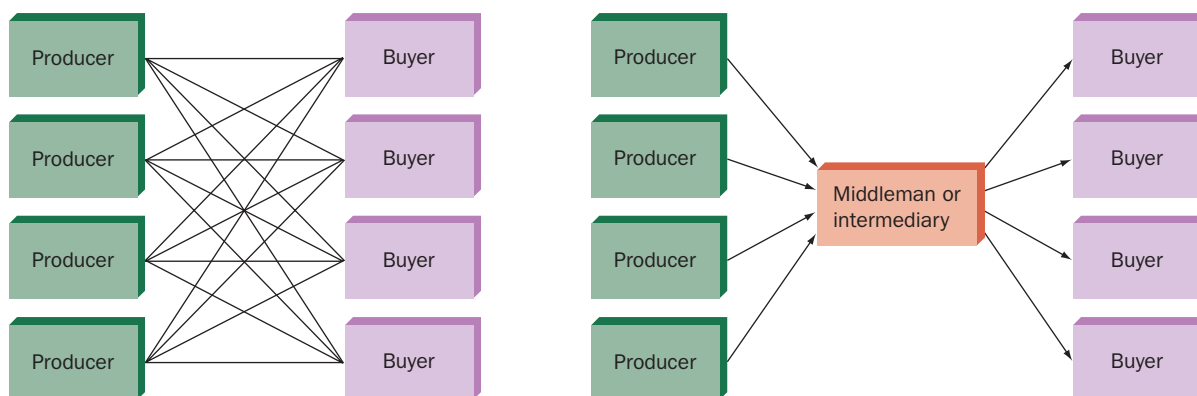
The press, consumers, public officials, and other marketers often charge wholesalers, at least in principle, with inefficiency and parasitism. Consumers in particular feel strongly that the distribution channel should be made as short as possible. They assume that the fewer the intermediaries in a distribution channel, the lower the price of the product will be.

Those who believe that the elimination of wholesalers will bring about lower prices, however, do not recognize that the services wholesalers perform are still needed. Those services simply are provided by other means, and consumers still bear the costs. Moreover, all manufacturers operating without wholesalers would have to keep extensive records and employ enough personnel to deal with a multitude of retailers individually. Even with direct distribution, products might be considerably more expensive because prices would reflect the costs of producers' inefficiencies. Figure 14.3 shows that 16 contacts could result from the efforts of four buyers purchasing the products of four producers. With the assistance of an intermediary, only eight contacts would be necessary.

To illustrate further the useful role of wholesalers in the marketing system, assume that all wholesalers in the candy industry were abolished. With thousands of candy retailers to contact, candy manufacturers would be making an extremely large number of sales calls just to maintain the present level of product visibility. Hershey Foods, for example, would have to set up warehouses all over the country, organize a fleet of trucks, purchase and maintain thousands of vending machines, and deliver all its own candy. Sales and distribution costs for candy would soar. Candy producers would be contacting and shipping products to thousands of small businesses instead of to a limited number of large wholesalers and retailers. The outrageous costs of this inefficiency would be passed on to consumers. Candy bars would be more expensive and likely available through fewer retailers.

Wholesalers often are more efficient and economical not only for manufacturers, but also for consumers. Because pressure to eliminate them comes from both

The services of an intermediary reduce the number of contacts, or exchanges, between producers and buyers, thereby increasing efficiency.



Source: William M. Pride and O.C. Ferrell, *Marketing: Concepts and Strategies*, 16 ed. (Mason, OH: South-Western/Cengage Learning, 2012). Adapted with permission.

ends of the marketing channel, wholesalers should perform only those functions that are genuinely in demand. To stay in business, wholesalers also should take care to be efficient and productive and to provide high-quality services to other channel members.

### Wholesalers' Services to Retailers

Wholesalers help retailers by buying in large quantities and then selling to retailers in smaller quantities and by delivering goods to retailers. They also stock—in one place—the variety of goods that retailers otherwise would have to buy from many producers. Wholesalers provide assistance in three other vital areas: promotion, market information, and financial aid.

**Promotion** Some wholesalers help to promote the products they sell to retailers. These services are usually either free or performed at cost. Wholesalers, for example, are major sources of display materials designed to stimulate impulse buying. They also may help retailers to build effective window, counter, and shelf displays. Some may even assign their own employees to work on the retail sales floor during special promotions.

**Market Information** Wholesalers are a constant source of market information. Wholesalers have numerous contacts with local businesses and distant suppliers. In the course of these dealings, they accumulate information about consumer demand, prices, supply conditions, new developments within the trade, and even industry personnel. This information may be relayed to retailers informally through the wholesaler's sales force. Some wholesalers also provide information to their customers through Web sites.

Information regarding industry sales and competitive prices is especially important to all firms. Dealing with a number of suppliers and many retailers, a wholesaler is a natural clearinghouse for such information. Most wholesalers are willing to pass information on to their customers.

**Financial Aid** Most wholesalers provide a type of financial aid that retailers often take for granted. By making prompt and frequent deliveries, wholesalers enable retailers to keep their own inventory investments small in relation to sales. Such indirect financial aid reduces the amount of operating capital that retailers need.



## Wholesalers' Services to Manufacturers

Some of the services that wholesalers perform for producers are similar to those they provide to retailers. Others are quite different.

**Providing an Instant Sales Force** A wholesaler provides its producers with an instant sales force so that producers' sales representatives need not call on retailers. This can result in enormous savings for producers. For example, Lever Brothers and General Foods would have to spend millions of dollars each year to field a sales force large enough to call on all the retailers that sell their numerous products. Instead, these producers rely on wholesalers to sell and distribute their products to many retailers. These producers do have sales forces, though, that call on wholesalers and large retailers.

**Reducing Inventory Costs** Wholesalers purchase goods in sizable quantities from manufacturers and store these goods for resale. By doing so, they reduce the amount of finished-goods inventory that producers must hold and thereby reduce the cost of carrying inventories.

**Assuming Credit Risks** When producers sell through wholesalers, it is the wholesalers who extend credit to retailers, make collections from retailers, and assume the risks of non-payment. These services reduce the producers' cost of extending credit to customers and the resulting bad-debt expense.

**Furnishing Market Information** Just as they do for retailers, wholesalers supply market information to the producers they serve. Valuable information accumulated by wholesalers may concern consumer demand, the producers' competition, and buying trends.

**merchant wholesaler** a middleman that purchases goods in large quantities and then sells them to other wholesalers or retailers and to institutional, farm, government, professional, or industrial users

## Types of Wholesalers

Wholesalers generally fall into three categories: merchant wholesalers; commission merchants, agents, and brokers; and manufacturers' sales branches and sales offices. Of these, merchant wholesalers constitute the largest portion. They account for about four-fifths of all wholesale establishments and employees.

**Merchant Wholesalers** A **merchant wholesaler** is a middleman that purchases goods in large quantities and then sells them to other wholesalers or retailers and to institutional, farm, government, professional, or industrial users. Merchant wholesalers usually operate one or more warehouses at which they receive, take title to, and store goods. These wholesalers are sometimes called *distributors* or *jobbers*.

Most merchant wholesalers are businesses composed of salespeople, order takers, receiving and shipping clerks, inventory managers, and office personnel. The successful merchant wholesaler must analyze available products and market needs. It must be able to adapt the type, variety, and quality of its products to changing market conditions.

Merchant wholesalers may be classified as full-service or limited-service wholesalers, depending on the number of services they provide. A **full-service wholesaler** performs the entire range of wholesaler functions described earlier in this section. These functions include delivering goods, supplying, warehousing, arranging for credit, supporting promotional activities, and providing general customer assistance.

6 Identify and describe the major types of wholesalers.

**full-service wholesaler** a middleman that performs the entire range of wholesaler functions



**General merchandise wholesaler.** A general merchandise wholesaler carries a broad product mix.

Under this broad heading are the general-merchandise wholesaler, limited-line wholesaler, and specialty-line wholesaler. A **general-merchandise wholesaler** deals in a wide variety of products, such as drugs, hardware, nonperishable foods, cosmetics, detergents, and tobacco. A **limited-line wholesaler** stocks only a few product lines but carries numerous product items within each line. A **specialty-line wholesaler** carries a select group of products within a single line. Food delicacies such as shellfish represent the kind of product handled by this type of wholesaler.

In contrast to a full-service wholesaler, a **limited-service wholesaler** assumes responsibility for a few wholesale services only. Other marketing tasks are left to other channel members or consumers. This category includes cash-and-carry wholesalers, truck wholesalers, drop shippers, and mail-order wholesalers.

**Commission Merchants, Agents, and Brokers** Commission merchants, agents, and brokers are functional middlemen. Functional middlemen do not take title to products. They perform a small number of marketing activities and are paid a commission that is a percentage of the sales price.

A **commission merchant** usually carries merchandise and negotiates sales for manufacturers. In most cases, commission merchants have the power to set the prices and terms of sales. After a sale is made, they either arrange for delivery or provide transportation services.

An **agent** is a middleman that expedites exchanges, represents a buyer or a seller, and often is hired permanently on a commission basis. When agents represent producers, they are known as *sales agents* or *manufacturer's agents*. As long as the products represented do not compete, a sales agent may represent one or several manufacturers on a commission basis. The agent solicits orders for the manufacturers within a specific territory. As a rule, the manufacturers ship the merchandise and bill the customers directly. The manufacturers also set the prices and other conditions of the sales. What do the manufacturers gain by using a sales agent? The sales agent provides immediate entry into a territory, regular calls on customers, selling experience, and a known, predetermined selling expense (a commission that is a percentage of sales revenue).

A **broker** is a middleman that specializes in a particular commodity, represents either a buyer or a seller, and is likely to be hired on a temporary basis. However, food brokers, which sell grocery products to resellers, generally have long-term relationships with their clients. Brokers may perform only the selling function, or both buying and selling, using established contacts or special knowledge of their fields.

**Manufacturers' Sales Branches and Sales Offices** A **manufacturer's sales branch** is, in essence, a merchant wholesaler that is owned by a manufacturer. Sales branches carry inventory, extend credit, deliver goods, and offer help in promoting products. Their customers are retailers, other wholesalers, and industrial purchasers.

Because sales branches are owned by producers, they stock primarily the goods manufactured by their own firms. Selling policies and terms usually are established centrally and then transmitted to branch managers for implementation.

A **manufacturer's sales office** is essentially a sales agent owned by a manufacturer. Sales offices may sell goods manufactured by their own firms as well as certain products of other manufacturers that complement their own product lines. For example, Hiram Walker & Sons imports wine from Spain to increase the number of products its sales offices can offer to customers.

**general-merchandise wholesaler** a middleman that deals in a wide variety of products

**limited-line wholesaler** a middleman that stocks only a few product lines but carries numerous product items within each line

**specialty-line wholesaler** a middleman that carries a select group of products within a single line

**limited-service wholesaler** a middleman that assumes responsibility for a few wholesale services only

**commission merchant** a middleman that carries merchandise and negotiates sales for manufacturers

**agent** a middleman that expedites exchanges, represents a buyer or a seller, and often is hired permanently on a commission basis

**broker** a middleman that specializes in a particular commodity, represents either a buyer or a seller, and is likely to be hired on a temporary basis

**manufacturer's sales branch** essentially a merchant wholesaler that is owned by a manufacturer

**manufacturer's sales office** essentially a sales agent owned by a manufacturer

## 7

Distinguish among the major types of retailers.

## Marketing Intermediaries: Retailers

Retailers are the final link between producers and consumers. Retailers may buy from either wholesalers or producers. They sell not only goods but also such services as auto repairs, haircuts, and dry cleaning. Some retailers sell both. Sears, Roebuck and Company sells consumer goods, financial services, and repair services for home appliances bought at Sears.

Of approximately 2.6 million retail firms in the United States, about 90 percent have annual sales of less than \$1 million. On the other hand, some large retail organizations realize well over \$1 million in sales revenue per day. Table 14.1 lists the ten largest retail organizations and their approximate sales revenues and yearly profits.

### Classes of In-Store Retailers

One way to classify retailers is by the number of stores owned and operated by the firm. An **independent retailer** is a firm that operates only one retail outlet. Approximately three-fourths of retailers are independent. One-store operators, like all small businesses, generally provide personal service and a convenient location.

A **chain retailer** is a company that operates more than one retail outlet. By adding outlets, chain retailers attempt to reach new geographic markets. As sales increase, chains usually buy merchandise in larger quantities and thus take advantage of quantity discounts. They also wield more power in their dealings with suppliers. About one-fourth of retail organizations operate chains.

Another way to classify in-store retailers is by store size and the kind and number of products carried. Let's take a closer look at store types based on these dimensions.



**Retailing.** Retailing occurs in brick-and-mortar establishments, online, at home, and in the workplace.

**Department Stores** These large retail establishments consist of several sections, or departments, that sell a wide assortment of products. According to the U.S. Bureau of the Census, a **department store** is a retail store that (1) employs 25 or more persons and (2) sells at least home furnishings, appliances, family apparel, and household linens and dry goods, each in a different part of the store. Marshall Field's in Chicago (and several other cities), Harrods in London, and Au Printemps in Paris are examples of large department stores. Sears, Roebuck and JCPenney are also department stores. Traditionally, department stores have been service oriented. Along with the goods they sell, these retailers provide credit, delivery, personal assistance, liberal return policies, and pleasant shopping atmospheres.

**Discount Stores** A **discount store** is a self-service general-merchandise outlet that sells products at lower-than-usual prices. These stores can offer lower prices by operating on smaller markups, by locating large retail showrooms in low-rent areas,

**Table 14.1** Top Ten Largest U.S. Retailers

Rank	Company	Revenues (000)	Earnings (000)	No. of Stores
1	Walmart	\$405,607,000	\$13,400,000	7,873
2	CVS Caremark	\$ 87,471,900	\$ 3,212,100	6,981
3	Kroger	\$ 76,000,000	\$ 1,249,000	3,654
4	Costco	\$ 72,483,020	\$ 1,282,725	544
5	Home Depot	\$ 71,288,000	\$ 2,260,000	2,274
6	Target	\$ 64,948,000	\$ 2,214,000	1,682
7	Walgreens	\$ 59,034,000	\$ 2,157,000	6,934
8	Lowe's	\$ 48,230,000	\$ 2,157,000	1,649
9	Sears Holdings	\$ 46,770,000	\$ 53,000	3,918
10	Best Buy	\$ 45,015,000	\$ 1,003,000	3,942

Source: "Top 100 Retailers," *Stores*, July 2009, <http://www.stores.org/2009/Top-100-Retailers>. Reprinted with permission from Wrights Reprints.

**independent retailer** a firm that operates only one retail outlet

**chain retailer** a company that operates more than one retail outlet

**department store** a retail store that (1) employs 25 or more persons and (2) sells at least home furnishings, appliances, family apparel, and household linens and dry goods, each in a different part of the store

**discount store** a self-service general-merchandise outlet that sells products at lower-than-usual prices

© iStockphoto.com/Tibor Nagy

and by offering minimal customer services. To keep prices low, discount stores operate on the basic principle of high turnover of such items as appliances, toys, clothing, automotive products, and sports equipment. To attract customers, many discount stores also offer some food and household items at low prices. Popular discount stores include Kmart, Walmart, Dollar General, and Target.

As competition among discount stores has increased, some discounters have improved their services, store environments, and locations. As a consequence, many of the better-known discount stores have assumed the characteristics of department stores. This upgrading has boosted their prices and blurred the distinction between some discount stores and department stores.

**Catalog and Warehouse Showrooms** A **catalog showroom** is a retail outlet that displays well-known brands and sells them at discount prices through catalogs within the store. Colorful catalogs are available in the showroom (and sometimes by mail). The customer selects the merchandise, either from the catalog or from the showroom display. The customer fills out an order form provided by the store and hands the form to a clerk. The clerk retrieves the merchandise from a warehouse room that is adjacent to the selling area. Service Merchandise is a catalog showroom.

A **warehouse showroom** is a retail facility with five basic characteristics: (1) a large, low-cost building; (2) warehouse materials-handling technology; (3) vertical merchandise displays; (4) a large on-premises inventory; and (5) minimal service. Some of the best-known showrooms are operated by big furniture retailers. These operations employ few personnel and offer few services. Most customers carry away purchases in the manufacturer's carton, although some warehouse showrooms will deliver for a fee.

**Convenience Stores** A **convenience store** is a small food store that sells a limited variety of products but remains open well beyond normal business hours. Almost 70 percent of convenience store customers live within a mile of the store. White Hen Pantry, 7-Eleven, Circle K, and Open Pantry stores, for example, are found in some areas, as are independent convenience stores. There are over 117,000 convenience stores in the United States.<sup>4</sup> Their limited product mixes and higher prices keep convenience stores from becoming a major threat to other grocery retailers.

**Supermarkets** A **supermarket** is a large self-service store that sells primarily food and household products. It stocks canned, fresh, frozen, and processed foods; paper products; and cleaning supplies. Supermarkets also may sell such items as housewares, toiletries, toys and games, drugs, stationery, books and magazines, plants and flowers, and a few clothing items.

Supermarkets are large-scale operations that emphasize low prices and one-stop shopping for household needs. A supermarket has annual sales of at least \$2 million. Current top-ranking supermarkets include Kroger, Albertson's, Safeway, Winn-Dixie, and A&P. Many of these supermarket chains are finding it difficult to compete with superstores such as Walmart Supercenters and are experiencing minuscule profit margins. Walmart, for example, expects to generate in its "supermarket-type" stores more revenue than the top three U.S. supermarket chains—Kroger, Albertson's, and Safeway—combined.

**Superstores** A **superstore** is a large retail store that carries not only food and nonfood products ordinarily found in supermarkets but also additional product lines—housewares, hardware, small appliances, clothing, personal-care products, garden products, and automotive merchandise. Superstores also provide a number of services to entice customers. Typically, these include automotive repair, snack bars and restaurants, film developing, and banking.

**catalog showroom** a retail outlet that displays well-known brands and sells them at discount prices through catalogs within the store

**warehouse showroom** a retail facility in a large, low-cost building with a large on-premises inventory and minimal service

**convenience store** a small food store that sells a limited variety of products but remains open well beyond normal business hours

**supermarket** a large self-service store that sells primarily food and household products

**superstore** a large retail store that carries not only food and nonfood products ordinarily found in supermarkets but also additional product lines



**Warehouse Clubs** The **warehouse club** is a large-scale members-only establishment that combines features of cash-and-carry wholesaling with discount retailing. For a nominal annual fee (about \$25), small retailers may purchase products at wholesale prices for business use or for resale. Warehouse clubs also sell to ultimate consumers. Instead of paying a membership fee, individual consumers pay about 5 percent more on each item than do small-business owners. Individual purchasers can usually choose to pay yearly dues for membership cards that allow them to avoid the 5 percent additional charge.

Warehouse clubs offer the same types of products offered by discount stores but in a limited range of sizes and styles. Because their product lines are shallow and sales volumes are high, warehouse clubs can offer a broad range of merchandise, including perishable and nonperishable foods, beverages, books, appliances, housewares, automotive parts, hardware, furniture, and sundries. The sales volume of most warehouse clubs is four to five times that of a typical department store. With stock turning over at an average rate of 18 times each year, warehouse clubs sell their goods before manufacturers' payment periods are up, thus reducing their need for capital.

To keep their prices 20 to 40 percent lower than those of supermarkets and discount stores, warehouse clubs provide few services. They generally advertise only through direct mail. Their facilities often have concrete floors and aisles wide enough for forklifts. Merchandise is stacked on pallets or displayed on pipe racks. Usually customers must transport purchases themselves. Although at one time there were about 20 competing warehouse clubs, only two major competitors remain: Sam's Club and Costco. Sam's Club stores stock about 4,000 items, with 1,400 available most of the time and the rest being one-time buys. Costco leads the warehouse club industry with sales of \$71.4 billion. Sam's Club is second with nearly \$47 billion in store sales.<sup>5</sup>

**Traditional Specialty Stores** A **traditional specialty store** carries a narrow product mix with deep product lines. Traditional specialty stores are sometimes called *limited-line retailers*. If they carry depth in one particular product category, they may be called *single-line retailers*. Specialty stores usually sell such products as clothing, jewelry, sporting goods, fabrics, computers, flowers, baked goods, books, and pet supplies. Examples of specialty stores include Gap Inc., Radio Shack, Bath and Body Works, and Foot Locker.

Specialty stores usually offer deeper product mixes than department stores. They attract customers by emphasizing service, atmosphere, and location. Consumers who are dissatisfied with the impersonal atmosphere of large retailers often find the attention offered by small specialty stores appealing.

**warehouse club** a large-scale members-only establishment that combines features of cash-and-carry wholesaling with discount retailing

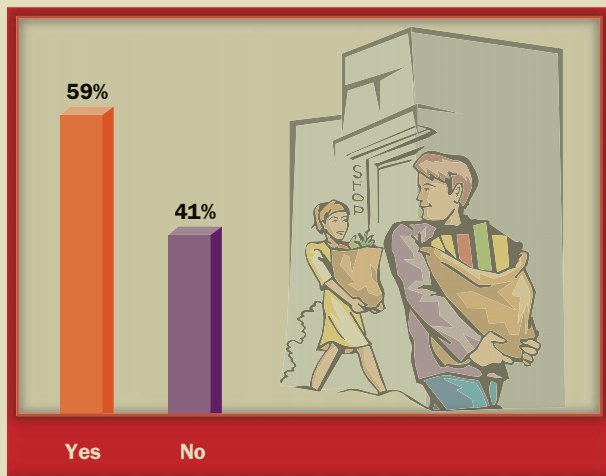
**traditional specialty store** a store that carries a narrow product mix with deep product lines



**Warehouse clubs.** Costco is an example of a warehouse club.

© Food Market Institute  
© Justin Sullivan/Getty Images

## Will You Pay More for a Luxury Item at a Brand Store than at a Discount Store?



Source: Accenture Consumer Luxury survey of 1,002 adults.

**off-price retailer** a store that buys manufacturers' seconds, overruns, returns, and off-season merchandise for resale to consumers at deep discounts

**category killer** a very large specialty store that concentrates on a single product line and competes on the basis of low prices and product availability

ics), all of which are leaders in their niche. Toys“R”Us, one of the original category killers, has a bleak future; the inability to maintain high sales year round with a market that focuses on the holidays has had its effect on the toy retailer. Many category killers, including Toys“R”Us, are experiencing lower sales as they struggle to compete with Walmart, the world’s number one retailer, which can price goods below cost and easily shift the concentration of different categories of goods in its stores depending on the store’s location and the time of the year.<sup>6</sup>



**Traditional specialty store.** A traditional specialty store carries one product line with considerable depth. This clothing store is a traditional specialty store.

**Off-Price Retailers** An **off-price retailer** is a store that buys manufacturers’ seconds, overruns, returns, and off-season merchandise at below-wholesale prices and sells them to consumers at deep discounts. Off-price retailers sell limited lines of national-brand and designer merchandise, usually clothing, shoes, or housewares. Examples of off-price retailers include T.J.Maxx, Burlington Coat Factory, and Marshalls. Off-price stores charge up to 50 percent less than department stores do for comparable merchandise but offer few customer services. They often include community dressing rooms and central checkout counters, and some off-price retailers have a no-returns, no-exchanges policy.

**Category Killers** A **category killer** is a very large specialty store that concentrates on a single product line and competes by offering low prices and an enormous number of products. These stores are called *category killers* because they take business away from smaller, high-cost retail stores. Examples of category killers include Home Depot (building materials), Office Depot (office supplies and equipment), and Best Buy (electronics), all of which are leaders in their niche.

### Kinds of Nonstore Retailing

**Nonstore retailing** is selling that does not take place in conventional store facilities; consumers purchase products without visiting a store. This form of retailing accounts for an increasing percentage of total retail sales. Nonstore retailers use direct selling, direct marketing, and vending machines.

**Direct Selling** **Direct selling** is the marketing of products to customers through face-to-face sales presentations at home or in the workplace. Traditionally called *door-to-door selling*, direct selling in the United States began with peddlers more than a century ago and has since grown into a sizable industry that generates about \$30 billion in U.S. sales annually.<sup>7</sup> Instead of the door-to-door approach, many companies today—such as Mary Kay, Kirby, Amway, and Avon—use other approaches. They identify customers by mail, telephone, the Internet, or at shopping malls and then set up appointments. Direct selling sometimes involves the “party plan,”

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# Going for SUCCESS

## Major Brands Party at Home

Shop at home has taken on a new meaning as major brands test direct selling through the party plan. All kinds of goods and services are being marketed in homes worldwide these days, including DiGiorno frozen pizza, Purina pet food, Verizon fiber-optic communications services, and Microsoft software.

When Microsoft introduced its Windows 7 operating system, the company hired a company called House Party to recruit hosts for parties across the United States, in Europe, and in Asia. To see how the program worked, Microsoft's executives started by holding their own house parties. They were surprised at how receptive participants were to the new product. "They thanked us," says Microsoft's

top marketing official, adding that guests welcomed the party plan as "a refreshing change" from the typical marketing campaign.

More than 50,000 hosts participated in the Windows 7 party plan. Microsoft provided each host with a free copy of the software, a tote bag, a deck of cards, and party favors. Hosts enjoyed the status of being among the first to own the software. Guests liked being able to preview the new software and discuss it with friends in a relaxed, party atmosphere. Just as important, the photographs, videos, blog entries, and tweets posted online by hosts and guests kept the positive buzz going strong long after the parties were over.

Sources: Andrew McMains, "Consumers Party on for Major Brands," *Adweek*, February 1, 2010, <http://www.adweek.com>; Laurie Burkitt, "Marketers Break into Homes by Sponsoring Parties," *Forbes*, August 19, 2009, <http://www.forbes.com>; Christina Cheddar Berk, "Building Buzz: It's Not Just About Free Pizza," *CNBC*, January 26, 2010, <http://www.cnbc.com>.

which can occur in the customer's home or workplace. One customer will act as a host and invite friends and co-workers to view merchandise in a group setting where the salesperson demonstrates the products. Direct selling through the party plan requires effective salespeople who can identify potential hosts and provide encouragement and incentives for them to organize a gathering of friends and associates. Companies that commonly use the party plan are Tupperware, Stanley Home Products, Pampered Chef, and Sarah Coventry. Mary Kay also uses the party plan by holding group pajama parties, makeovers, and girls' nights out.

Direct selling has both benefits and limitations. It gives the marketer an opportunity to demonstrate the product in an environment—usually customers' homes—where it most likely would be used. Some companies, such as Kirby Vacuums, will even clean the carpet in your home while they demonstrate their product. The direct seller can give the customer personal attention, and the product can be presented to the customer at a convenient time and location. Personal attention to the customer is the foundation on which some direct sellers have built their businesses. For example, your Mary Kay salesperson can recommend beauty and skin products tailored to your special needs. Because commissions are so high, ranging from 30 to 50 percent of the sales price, and great effort is required to isolate promising prospects, overall costs of direct selling make it a very expensive form of retailing. Furthermore, some customers view direct selling negatively owing to unscrupulous and fraudulent practices used by some direct sellers in the past. Some communities even have local ordinances that control or, in some cases, prohibit door-to-door selling.

**Direct Marketing** **Direct marketing** is the use of the telephone, Internet, and nonpersonal media to communicate product and organizational information to customers, who can then purchase products via mail, telephone, or the Internet. Direct marketing is one type of nonstore retailing. Direct marketing can occur through catalog marketing, direct-response marketing, telemarketing, television home shopping, and online marketing.

**nonstore retailing** a type of retailing whereby consumers purchase products without visiting a store

**direct selling** the marketing of products to customers through face-to-face sales presentations at home or in the workplace

**direct marketing** the use of the telephone, Internet, and nonpersonal media to introduce products to customers, who can then purchase them via mail, telephone, or the Internet



**Category killer.** Best Buy is an example of a category killer.

**storage & display**  
Stylish solutions for organizing your home

**Direct marketing.** Some retailers like Pottery Barn have brick-and-mortar stores and also use direct marketing such as catalog and online retailing.

In **catalog marketing**, an organization provides a catalog from which customers make selections and place orders by mail, telephone, or the Internet. Catalog marketing began in 1872, when Montgomery Ward issued its first catalog to rural families. Today, there are more than 7,000 catalog marketing companies in the United States, as well as a number of retail stores, such as Chico's, that engage in catalog marketing. Some organizations, including Spiegel, offer a broad array of products spread over multiple product lines. JCPenney historically has used a similar approach. However, JCPenney recently revamped its catalog strategy at the end of last year, doing away with "The Big Book," a 1,000-page catalog, and replacing it with smaller specialty catalogs.<sup>8</sup> Catalog companies such as Lands' End, Pottery Barn, and J.Crew offer considerable depth in one major line of products. Still other catalog companies specialize in only a few products within a single line. The advantages of catalog marketing include efficiency and convenience for customers. The retailer benefits by being able to locate in remote, low-cost areas; save on expensive store fixtures; and reduce both personal selling and store operating expenses. On the other hand, catalog marketing is inflexible, provides limited service, and is most effective for only a selected set of products.

Even though the cost of mailing catalogs continues to rise, catalog sales are growing at double the rate of in-store retailing. Williams-Sonoma, for example, sells kitchenware and home and garden products through five catalogs, including Pottery Barn and Gardeners' Eden. Catalog sales have been increasing owing to the convenience of catalog shopping. Product quality is often high, and because consumers can call toll-free 24 hours a day or order online, charge purchases to a credit card, and have the merchandise delivered to their door in one to two days, such shopping is much easier than going to a store.

**Direct-response marketing** occurs when a seller advertises a product and makes it available, usually for a short time period, through mail, telephone, or online orders. Examples of direct-response marketing include a television commercial offering a recording artist's musical collection, or a newspaper or magazine advertisement for a series of children's books. One of the most successful direct-response initiatives in the past few years was for the Snuggie. This product was first introduced on late-night TV, and became so popular through direct-response marketing that it eventually made its way into retail outlets like Bed Bath & Beyond, Walgreens, and eventually pet stores like PetSmart when the Snuggie for dogs was created. The company sold 5 million Snuggies its first year and expects to sell 20 million this year.<sup>9</sup> In general, products must be priced above \$20 to justify the advertising and distribution costs associated with direct-response marketing.

**Telemarketing** is the performance of marketing-related activities by telephone. Some organizations use a prescreened list of prospective clients. Telemarketing can help generate sales leads, improve customer service, speed up payments on past-due accounts, raise funds for non-profit organizations, and gather marketing data.

Currently, the laws and regulations regarding telemarketing, while in a state of flux, are becoming more restrictive. Several states have established do-not-call lists of customers who do not want to receive telemarketing calls from companies. On October 1, 2003, the U.S. Congress implemented the national do-not-call registry for consumers who do not want to receive telemarketing calls. So far, the do-not-call registry listed about 200 million phone numbers. Regulations associated with the national do-not-call registry are enforced by the Federal Trade Commission

**catalog marketing** a type of marketing in which an organization provides a catalog from which customers make selections and place orders by mail, telephone, or the Internet

**direct-response marketing** a type of marketing in which a seller advertises a product and makes it available, usually for a short time period, through mail, telephone, or online orders

**telemarketing** the performance of marketing-related activities by telephone

© Newscom



(FTC). Companies are subject to fines of up to \$16,000 for each call made to consumers listed on the national do-not-call registry. Since the registry went into effect, the two federal agencies have collected \$21 million in penalties and \$12 million in restitution from violators. Companies can access data for up to five area codes for free. The annual fee telemarketers must pay to access the registry is \$55 for each additional area code of data accessed, with a maximum annual fee of \$15,058.<sup>10</sup> Certain exceptions apply to no-call lists. A company can still use telemarketing to communicate with existing customers. In addition, charitable, political, and telephone survey organizations are not restricted by the national registry.

**Television home shopping** presents products to television viewers, encouraging them to order through toll-free numbers and pay with credit cards. The Home Shopping Network (HSN) originated and popularized this format. The most popular products sold through television home shopping are jewelry (40 percent of total sales), clothing, housewares, and electronics. Home shopping channels have grown so rapidly in recent years that more than 60 percent of U.S. households have access to home shopping programs. HSN and QVC are two of the largest home shopping networks. With the growing popularity of this medium, new channels are being added, even ones that specialize in one specific product category, such as Jewelry Television. Approximately 60 percent of home shopping sales revenues come from repeat purchasers.

The television home shopping format offers several benefits. Products can be demonstrated easily, and an adequate amount of time can be spent showing the product so as to make viewers well informed. The length of time a product is shown depends not only on the time required for doing the demonstration but also on whether the product is selling. Once the calls peak and begin to decline, a new product is shown. Another benefit is that customers can shop at their convenience from the comfort of their homes.

**Online retailing** makes products available to buyers through computer connections. Most brick-and-mortar retailers have Web sites to sell products, provide information about their company, or distribute coupons. Consumers can also bid on anything from concert tickets, automobiles, or even a wedge of cheese shaped like Elvis on eBay. Netflix has changed the video rental industry by offering its completely online movie rental service.<sup>11</sup> Brokerage firms have established Web sites to give their customers direct access to manage their accounts and enable them to trade online. With advances in computer technology continuing and consumers ever more pressed for time, online retailing will continue to escalate. This trend is evident when looking at sales from Black Friday, the Friday after Thanksgiving when most retailers drastically mark down products to jump start the holiday shopping season. It is common to find customers camping outside of retail stores to take advantage of the huge discounts. This trend may be dwindling as many consumers decide to sleep in and take advantage of the price reductions from their computer at home. Last year, online sales were up 11 percent on Black Friday.<sup>12</sup> Although online retailing represents a major retailing venue, security remains an issue. The threat of identity theft or credit card theft worries some online customers.

**Automatic Vending** **Automatic vending** is the use of machines to dispense products. It accounts for less than 2 percent of all retail sales. Automatic vending is one of the most impersonal forms of retailing. Small, standardized, routinely purchased products (e.g., chewing gum, candy, newspapers, cigarettes, soft drinks, and coffee) can be sold in machines because consumers usually buy them at the nearest available location. RedBox vending machines have started a new trend in vending, DVD rentals. These machines allow customers to rent DVDs at a time that is convenient for them, without a membership and from their choice of over 15,400 locations.<sup>13</sup> Machines in areas of heavy foot traffic provide efficient and continuous service to consumers. Such high-volume areas may have more diverse product availability—for example, hot and cold sandwiches, DVD rentals, or even iPods (yes, \$200 iPods are

**television home shopping** a form of selling in which products are presented to television viewers, who can buy them by calling a toll-free number and paying with a credit card

**online retailing** retailing that makes products available to buyers through computer connections

**automatic vending** the use of machines to dispense products

Identify the categories of shopping centers and the factors that determine how shopping centers are classified.

**lifestyle shopping center** an open-air-environment shopping center with upscale chain specialty stores

**neighborhood shopping center** a planned shopping center consisting of several small convenience and specialty stores

**community shopping center** a planned shopping center that includes one or two department stores and some specialty stores, along with convenience stores



**Lifestyle shopping centers.** The Village of Rochester Hills shopping center is one example of a lifestyle shopping center.

available in machines with coin slots). San Francisco-based company Zoom Systems has expanded its vending machine offerings from snacks to digital cameras, iPods and iPod accessories, Sephora brand beauty products, Rosetta Stone language learning software, and Proactiv skin care products.<sup>14</sup>

Since vending machines need only a small amount of space and no sales personnel, this retailing method has some advantages over stores. These advantages are partly offset, however, by the high costs of equipment and frequent servicing and repairs.

## Planned Shopping Centers

The planned shopping center is a self-contained retail facility constructed by independent owners and consisting of various stores. Shopping centers are designed and promoted to serve diverse groups of customers with widely differing needs. The management of a shopping center strives for a coordinated mix of stores, a comfortable atmosphere, adequate parking, pleasant landscaping, and special events to attract customers. The convenience of shopping for most family and household needs in a single location is an important part of shopping-center appeal.

There are four types of planned shopping centers: lifestyle, neighborhood, community, or regional. Although shopping centers vary, each offers a complementary mix of stores for the purpose of generating consumer traffic.

### Lifestyle Shopping Centers

A **lifestyle shopping center** is a shopping center that has an open-air configuration and is occupied by upscale national chain specialty stores. The lifestyle center is more convenient than a traditional enclosed mall and offers the same quality of upscale retail, department stores, movie theaters, and dining. A strong emphasis is placed on the architecture of the center and creating a pleasant and “hip” shopping environment. Most lifestyle centers are found in affluent neighborhoods.<sup>15</sup> An example of a lifestyle center is the Mount Pleasant Towne Center in South Carolina. The outdoor shopping center has large chain stores ranging from Banana Republic and Jos. A. Bank Clothiers to Edward Jones Investments and GameStop, as well as a few local stores like Sweet Julep’s Candy & Gifts. Visitors can also find a Mt. Pleasant Police Substation and several restaurants in the shopping center.<sup>16</sup>

### Neighborhood Shopping Centers

A **neighborhood shopping center** typically consists of several small convenience and specialty stores. Businesses in neighborhood shopping centers might include small grocery stores, drugstores, gas stations, and fast-food restaurants. These retailers serve consumers who live less than ten minutes away, usually within a two- to three-mile radius of the stores. Because most purchases in the neighborhood shopping center are based on convenience or personal contact, these retailers generally make only limited efforts to coordinate promotional activities among stores in the shopping center.

### Community Shopping Centers

A **community shopping center** includes one or two department stores and some specialty stores, along with convenience stores. It attracts consumers from a wider geographic area who will drive longer distances to find products and specialty items unavailable in neighborhood shopping centers. Community shopping centers, which are carefully planned and coordinated, generate traffic with special events such as art exhibits, automobile shows, and sidewalk sales. The management of a community shopping center maintains a balance of tenants so that the center can offer wide product mixes and deep product lines.



## Furniture Store? That Used to Be Our Roller-Skating Rink!

It takes entrepreneurial spirit to see a cavernous roller-skating rink as a future furniture store. However, an out-of-the-ordinary location was part of the appeal for Mary Liz Curtin and Stephen Scannell, the husband-and-wife owners of Leon & Lulu, an upscale furniture shop in Clawsen, Michigan. Curtin and Scannell liked the size and character of the Ambassador Roller Rink, a local landmark that was more than 60 years old. Although they had to renovate it for its new purpose, they left the rink's original scoreboard and floor intact.

Since the store's grand opening in 2006, Curtin and Scannell have incorporated the rink's heritage into their marketing efforts. They put hundreds



of the old skates on display and, during busy sales, their employees skate around serving cookies to customers. The location has become a major draw, helping build the store's annual sales beyond \$2 million. "We get letters from people who thank us for keeping the history alive," Curtin says.

The Old Clock Shop is also unusual, located in an old-fashioned home with a wrap-around porch just a few steps from Main Street in Sisters, Oregon. The house complements master clockmaker Ed Beacham's inventory of hand-crafted clocks and adds to the word of mouth about his store. The town attracts thousands of visitors during tourist season, and customers from as far away as New Zealand find their way to Beacham's unique store, ready to pay up to \$30,000 for his one-of-a-kind clocks.

Sources: Sarah E. Needleman, "Entrepreneurs Make Use of Odd Spaces," *The Wall Street Journal*, May 4, 2010, <http://www.wsj.com>; Kristian Foden-Vencil, "The Old Clock Shop Thrives in Sisters," *Oregon Public Broadcasting*, May 11, 2010, <http://news.opb.org/article/7278-clock-shop/>; <http://leonandlulu.com>.

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## Regional Shopping Centers

A **regional shopping center** usually has large department stores, numerous specialty stores, restaurants, movie theaters, and sometimes even hotels. It carries most of the merchandise offered by a downtown shopping district. Downtown merchants, in fact, often have renovated their stores and enlarged their parking facilities to meet the competition of successful regional shopping centers. Urban expressways and improved public transportation also have helped many downtown shopping areas to remain vigorous.

Regional shopping centers carefully coordinate management and marketing activities to reach the 150,000 or more customers in their target market. These large centers usually advertise, hold special events, and provide transportation to certain groups of customers. They also maintain a suitable mix of stores. National chain stores can gain leases in regional shopping centers more easily than small independent stores because they are better able to meet the centers' financial requirements.

**regional shopping center** a planned shopping center containing large department stores, numerous specialty stores, restaurants, movie theaters, and sometimes even hotels

## Physical Distribution

**Physical distribution** is all those activities concerned with the efficient movement of products from the producer to the ultimate user. Physical distribution therefore is the movement of the products themselves—both goods and services—through their channels of distribution. It is a combination of several interrelated business functions. The most important of these are inventory management, order processing, warehousing, materials handling, and transportation.

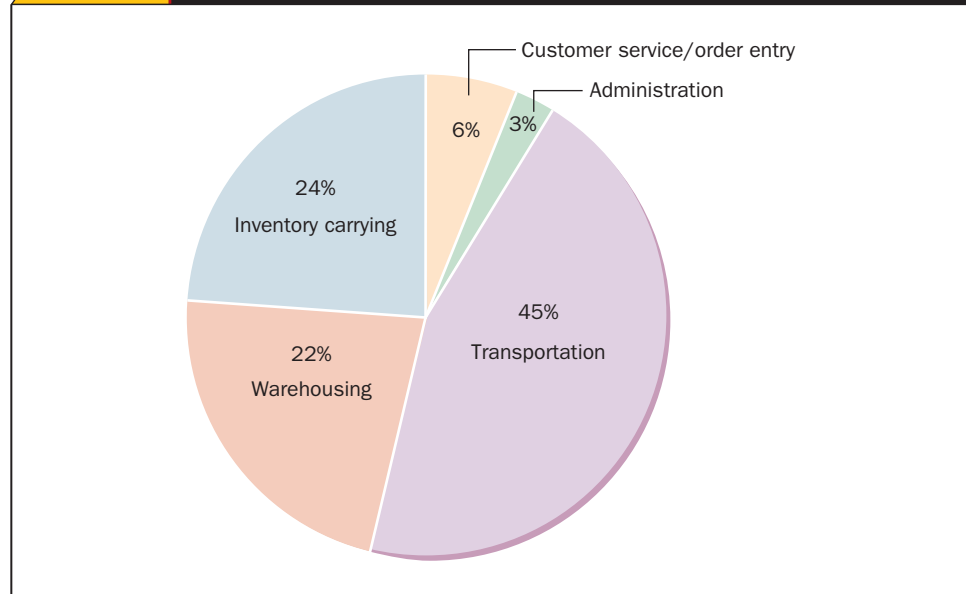
Not too long ago, each of these functions was considered distinct from all the others. In a fairly large firm, one group or department would handle each function.

9

Explain the five most important physical distribution activities.

**physical distribution** all the activities concerned with the efficient movement of products from the producer to the ultimate user

**Figure 14.4** Proportional Cost of Each Physical Distribution Function as a Percentage of Total Distribution Costs



Source: From Davis Database, 2005. Reprinted by permission of Establish Inc./Herbert W. David and Company.

Each of these groups would work to minimize its own costs and to maximize its own effectiveness, but the result was usually high physical distribution costs.

Various studies of the problem emphasized both the interrelationships among the physical distribution functions and the relationships between physical distribution and other marketing functions. Long production runs may reduce per-unit product costs, but they can cause inventory-control and warehousing costs to skyrocket. A new automated warehouse may reduce materials-handling costs, but if the warehouse is not located properly, transportation time and costs may increase substantially.

Because of such interrelationships, marketers now view physical distribution as an integrated effort that provides important marketing functions: getting the right product to the right place at the right time and at minimal overall cost. Figure 14.4 shows the proportional costs of each of the major physical distribution functions.

**inventory management** the process of managing inventories in such a way as to minimize inventory costs, including both holding costs and potential stock-out costs

## Inventory Management

In Chapter 8 we discussed inventory management from the standpoint of operations. We defined **inventory management** as the process of managing inventories in such a way as to minimize inventory costs, including both holding costs and potential stock-out costs. Both the definition and the objective of inventory control apply here as well.

*Holding costs* are the costs of storing products until they are purchased or shipped to customers. *Stock-out costs* are the costs of sales lost when items are not in inventory. Of course, holding costs can be reduced by minimizing inventories, but then stock-out costs could be financially threatening to the organization. Stock-out costs can be minimized by carrying very large inventories, but then holding costs would be enormous.

Inventory management, therefore, is a sort of balancing act between stock-out costs and holding costs. The latter include the cost of money invested in inventory, the cost of storage space, insurance costs, and inventory



**Inventory management technology.** This handheld inventory management device allows employees to have an instant overview of every item—and its price—in the warehouse at any given time.

© Marcin Balcerzak/Shutterstock.com

taxes. Often, even a relatively small reduction in inventory investment can provide a relatively large increase in working capital. Sometimes this reduction can best be accomplished through a willingness to incur a reasonable level of stock-out costs.

Companies frequently rely on technology and software to help manage inventory. Efficient inventory management with accurate reorder points is crucial for firms that use a just-in-time (JIT) approach, in which supplies arrive just as they are needed for use in production or for resale. When using JIT, companies maintain low inventory levels and purchase products and materials in small quantities whenever they need them. Usually, there is no safety stock, and suppliers are expected to provide consistently high-quality products. JIT inventory management requires a high level of coordination between producers and suppliers, but it eliminates waste and reduces inventory costs significantly. This approach has been used successfully by many well-known firms, including Chrysler, Harley-Davidson, and Dell Computers, to reduce costs and boost customer satisfaction. When a JIT approach is used in a supply chain, suppliers often move close to their customers.

## Order Processing

**Order processing** consists of activities involved in receiving and filling customers' purchase orders. It may include not only the means by which customers order products but also procedures for billing and for granting credit.

Fast, efficient order processing is an important marketing service—one that can provide a dramatic competitive edge. The people who purchase goods for intermediaries are especially concerned with their suppliers' promptness and reliability in order processing. To them, promptness and reliability mean minimal inventory costs as well as the ability to order goods when they are needed rather than weeks in advance. The Internet is providing new opportunities for improving services associated with order processing.

## Warehousing

**Warehousing** is the set of activities involved in receiving and storing goods and preparing them for reshipment. Goods are stored to create time utility; that is, they are held until they are needed for use or sale. Warehousing includes the following activities:

- *Receiving goods*—The warehouse accepts delivered goods and assumes responsibility for them.
- *Identifying goods*—Records are made of the quantity of each item received. Items may be marked, coded, or tagged for identification.
- *Sorting goods*—Delivered goods may have to be sorted before being stored.
- *Dispatching goods to storage*—Items must be moved to specific storage areas, where they can be found later.
- *Holding goods*—The goods are kept in storage under proper protection until needed.
- *Recalling, picking, and assembling goods*—Items that are to leave the warehouse must be selected from storage and assembled efficiently.
- *Dispatching shipments*—Each shipment is packaged suitably and directed to the proper transport vehicle. Shipping and accounting documents are prepared.

A firm may use its own warehouses or rent space in public warehouses. A *private warehouse*, owned and operated by a particular firm, can be designed to serve the firm's specific needs. However, the organization must take on the task of financing the facility, determining the best location for it, and ensuring that it is used fully. Generally, only companies that deal in large quantities of goods can justify private warehouses. Some such companies are United Parcel Service (UPS), Walmart, and Sears.

*Public warehouses* offer their services to all individuals and firms. Most are huge one-story structures on the outskirts of cities, where rail and truck transportation are easily available. They provide storage facilities, areas for sorting and assembling shipments, and office and display spaces for wholesalers and retailers.

**order processing** activities involved in receiving and filling customers' purchase orders

**warehousing** the set of activities involved in receiving and storing goods and preparing them for reshipment

Public warehouses also will hold—and issue receipts for—goods used as collateral for borrowed funds.

Many organizations locate and design their warehouses not only to be cost-efficient but also to provide excellent customer service.

## Materials Handling

**Materials handling** is the actual physical handling of goods—in warehouses as well as during transportation. Proper materials-handling procedures and techniques can increase the usable capacity of a warehouse or that of any means of transportation. Proper handling can reduce breakage and spoilage as well.

Modern materials handling attempts to reduce the number of times a product is handled. One method is called *unit loading*. Several smaller cartons, barrels, or boxes are combined into a single standard-size load that can be handled efficiently by forklift, conveyor, or truck.

## Transportation

As a part of physical distribution, **transportation** is simply the shipment of products to customers. The greater the distance between seller and purchaser, the more important is the choice of the means of transportation and the particular carrier.

A firm that offers transportation services is called a **carrier**. A *common carrier* is a transportation firm whose services are available to all shippers. Railroads, airlines, and most long-distance trucking firms are common carriers. A *contract carrier* is available for hire by one or several shippers. Contract carriers do not serve the general public. Moreover, the number of firms they can handle at any one time is limited by law. A *private carrier* is owned and operated by the shipper.

In addition, a shipper can hire agents called *freight forwarders* to handle its transportation. Freight forwarders pick up shipments from the shipper, ensure that the goods are loaded on selected carriers, and assume responsibility for safe delivery of the shipments to their destinations. Freight forwarders can often group a number of small shipments into one large load (which is carried at a lower rate). This, of course, saves money for shippers.

The U.S. Postal Service offers *parcel post* delivery, which is used widely by mail-order houses. The Postal Service provides complete geographic coverage at the lowest rates, but it limits the size and weight of the shipments it will accept. UPS, a privately owned firm, also provides small-parcel services for shippers. Other privately owned carriers, such as Federal Express, DHL, and Airborne, offer fast—often overnight—parcel delivery both within and outside the United States. There are also many local parcel carriers, including specialized delivery services for various time-sensitive industries, such as publishing.

The six major criteria used for selecting transportation modes are compared in Table 14.2. Obviously, the *cost* of a transportation mode is important to marketers. At times, marketers choose higher-cost modes of transportation because of the benefits they provide. *Speed* is measured by the total time that a carrier possesses the products, including time required for pickup and delivery, handling, and movement between point of origin and destination. Usually, there is a direct relationship between cost and speed; that is, faster modes of transportation are more expensive. A transportation mode's *dependability* is determined by the consistency of service provided by that mode. *Load flexibility* is the degree to which a transportation mode can provide appropriate equipment and conditions for moving specific kinds of products and can be adapted for moving other kinds of products. For example, certain types of products may need controlled temperatures or humidity levels. *Accessibility* refers to a transportation mode's ability to move goods over

**materials handling** the actual physical handling of goods, in warehouses as well as during transportation

**transportation** the shipment of products to customers

**carrier** a firm that offers transportation services



**Containerization.** Containers facilitate the use of multiple modes of transportation, such as rail, truck, and waterway.

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**Table 14.2** Characteristics and Ratings of Transportation Modes by Selection Criteria

	Railroads	Trucks	Pipelines	Waterways	Airplanes
<b>Selection Criteria</b>					
Cost	Moderate	High	Low	Very low	Very high
Speed	Average	Fast	Slow	Very slow	Very fast
Dependability	Average	High	High	Average	High
Load Flexibility	High	Average	Very low	Very high	Low
Accessibility	High	Very high	Very limited	Limited	Average
Frequency	Low	High	Very high	Very low	Average
<b>% Ton-Miles Transported</b>	39.4	28.6	19.6	12.0	0.3
<b>Products Carried</b>	Coal, grain, lumber, heavy equipment, paper and pulp products, chemicals	Clothing, computers, books, groceries, produce, livestock	Oil, processed coal, natural gas	Chemicals, bauxite, grain, motor vehicles, agricultural implements	Flowers, food (highly perishable), technical instruments, emergency parts and equipment, overnight mail

Source: U.S. Bureau of Transportation Statistics, *National Transportation Statistics* (Washington, DC: U.S. Government Printing Office), April 2010, [http://www.bts.gov/publications/national\\_transportation\\_statistics/html/table\\_01\\_46a.html](http://www.bts.gov/publications/national_transportation_statistics/html/table_01_46a.html).

a specific route or network. *Frequency* refers to how often a marketer can ship products by a specific transportation mode. Whereas pipelines provide continuous shipments, railroads and waterways follow specific schedules for moving products from one location to another. In Table 14.2, each transportation mode is rated on a relative basis for these six selection criteria. In addition, Table 14.2 shows a breakdown by use of the five different modes of transportation.

**Railroads** In terms of total freight carried, railroads are America’s most important mode of transportation. They are also the least expensive for many products. Almost all railroads are common carriers, although a few coal-mining companies operate their own lines.

Many commodities carried by railroads cannot be transported easily by any other means. They include a wide range of foodstuffs, raw materials, and manufactured goods. Coal ranks first by a considerable margin. Other major commodities carried by railroads include grain, paper and pulp products, liquids in tank-car loads, heavy equipment, and lumber.

**Trucks** The trucking industry consists of common, contract, and private carriers. It has undergone tremendous expansion since the creation of a national highway system in the 1920s. Trucks can move goods to suburban and rural areas not served by railroads. They can handle freight quickly and economically, and they carry a wide range of shipments. Many shippers favor this mode of transportation because it offers door-to-door service, less stringent packaging requirements than ships and airplanes, and flexible delivery schedules.

Railroad and truck carriers have teamed up to provide a form of transportation called *piggyback*. Truck trailers are carried from city to city on specially equipped railroad flatcars. Within each city, the trailers are then pulled in the usual way by truck tractors.

**Airplanes** Air transport is the fastest but most expensive means of transportation. All certified airlines are common carriers. Supplemental or charter lines are contract carriers.

Because of the high cost, lack of airport facilities in many areas, and reliance on weather conditions, airlines carry less than 1 percent of all intercity freight. Only high-value or perishable items, such as flowers, aircraft parts, and pharmaceuticals or goods that are needed immediately, are usually shipped by air.

**Waterways** Cargo ships and barges offer the least expensive, but slowest, form of transportation. They are used mainly for bulky nonperishable goods such as chemicals, grain, motor vehicles, and large equipment. Of course, shipment by water is limited to cities located on navigable waterways.

**Pipelines** Pipelines are a highly specialized mode of transportation. They are used primarily to carry petroleum and natural gas. Pipelines have become more important as the nation's need for petroleum products has increased. Such products as semiliquid coal and wood chips can also be shipped through pipelines continuously, reliably, and with minimal handling.

In the next chapter, we discuss the fourth element of the marketing mix—promotion.

## return to inside business

### GameStop

GameStop is playing in a highly competitive retail game. Giant chain retailers such as Walmart, Toys“R”Us, and Best Buy not only stock the top video games and consoles, they often feature these items in “door buster” price promotions. As a result, GameStop’s game plan is to emphasize its extensive and diverse inventory, its user-friendly trade-in program, and the hundreds of value-priced used products available in each retail location.

To reach its target market of enthusiasts, casual gamers, and gift-givers, GameStop operates 1,400-square-foot stores in busy shopping centers and downtown areas. It keeps thousands

of items in stock at all times and has equipment set up in each store so customers can try games before they buy. Even as GameStop opens 400 new stores a year, it never stops expanding its retail Web site, so it is ready when the digital future arrives.

### Questions

1. What role does physical distribution play in GameStop’s marketing strategy?
2. How would you classify GameStop as an in-store retailer? What are the implications for its marketing efforts?

## SUMMARY

### Summary

#### 1 Identify the various channels of distribution that are used for consumer and industrial products.

A marketing channel is a sequence of marketing organizations that directs a product from producer to ultimate user. The marketing channel for a particular product is concerned with the transfer of ownership of that product. Merchant middlemen (merchants) actually take title to products, whereas functional middlemen simply aid in the transfer of title.

The channels used for consumer products include the direct channel from producer to consumer; the channel

from producer to retailer to consumer; the channel from producer to wholesaler to retailer to consumer; and the channel from producer to agent to wholesaler to retailer to consumer. There are two major channels of industrial products: (1) producer to user and (2) producer to agent middleman to user.

#### 2 Explain the concept of market coverage.

Channels and intermediaries are chosen to implement a given level of market coverage. Intensive distribution is the use of all available outlets for a product, providing the widest market coverage. Selective distribution



uses only a portion of the available outlets in an area. Exclusive distribution uses only a single retail outlet for a product in a large geographic area.

### 3 Understand how supply-chain management facilitates partnering among channel members.

Supply-chain management is a long-term partnership among channel members working together to create a distribution system that reduces inefficiencies, costs, and redundancies while creating a competitive advantage and satisfying customers. Cooperation is required among all channel members, including manufacturing, research, sales, advertising, and shipping. When all channel partners work together, delivery, scheduling, packaging, and other customer requirements are better met. Technology, such as bar coding and electronic data exchange (EDI), makes supply-chain management easier to implement.

### 4 Describe what a vertical marketing system is and identify the types of vertical marketing systems.

A VMS is a centrally managed system. It results when two or more channel members from different levels combine under one management. Administered, contractual, and corporate systems represent the three major types of VMSs.

### 5 Discuss the need for wholesalers and describe the services they provide to retailers and manufacturers.

Wholesalers are intermediaries that purchase from producers or other intermediaries and sell to industrial users, retailers, or other wholesalers. Wholesalers perform many functions in a distribution channel. If they are eliminated, other channel members—such as the producer or retailers—must perform these functions. Wholesalers provide retailers with help in promoting products, collecting information, and financing. They provide manufacturers with sales help, reduce their inventory costs, furnish market information, and extend credit to retailers.

### 6 Identify and describe the major types of wholesalers.

Merchant wholesalers buy and then sell products. Commission merchants and brokers are essentially agents and do not take title to the goods they distribute. Sales branches and offices are owned by the manufacturers they represent and resemble merchant wholesalers and agents, respectively.

### 7 Distinguish among the major types of retailers.

Retailers are intermediaries that buy from producers or wholesalers and sell to consumers. In-store retailers include department stores, discount stores, catalog and warehouse showrooms, convenience stores, supermarkets, superstores, warehouse clubs, traditional specialty stores, off-price retailers, and category killers. Nonstore retailers do not sell in conventional store facilities. Instead, they use direct selling, direct marketing, and automatic vending. Types of direct marketing include catalog marketing, direct-response marketing, telemarketing, television home shopping, and online retailing.

### 8 Identify the categories of shopping centers and the factors that determine how shopping centers are classified.

There are three major types of shopping centers: neighborhood, community, and regional. A center fits one of these categories based on its mix of stores and the size of the geographic area it serves.

### 9 Explain the five most important physical distribution activities.

Physical distribution consists of activities designed to move products from producers to ultimate users. Its five major functions are inventory management, order processing, warehousing, materials handling, and transportation. These interrelated functions are integrated into the marketing effort.

## Key Terms

You should now be able to define and give an example relevant to each of the following terms:

channel of distribution (or marketing channel) (401)	selective distribution (403)	general-merchandise wholesaler (408)	manufacturer's sales branch (408)
middleman (or marketing intermediary) (401)	exclusive distribution (404)	limited-line wholesaler (408)	manufacturer's sales office (408)
merchant middleman (401)	supply-chain management (404)	specialty-line wholesaler (408)	independent retailer (409)
functional middleman (401)	vertical channel integration (404)	limited-service wholesaler (408)	chain retailer (409)
retailer (402)	vertical marketing system (VMS) (404)	commission merchant (408)	department store (409)
wholesaler (402)	merchant wholesaler (407)	agent (408)	discount store (409)
intensive distribution (403)	full-service wholesaler (407)	broker (408)	catalog showroom (410)
			warehouse showroom (410)

convenience store (410)	direct selling (413)	automatic vending (415)	physical distribution (417)
supermarket (410)	direct marketing (413)	lifestyle shopping center (416)	inventory management (418)
superstore (410)	catalog marketing (414)	neighborhood shopping center (416)	order processing (419)
warehouse club (411)	direct-response marketing (414)	community shopping center (416)	warehousing (419)
traditional specialty store (411)	telemarketing (414)	regional shopping center (417)	materials handling (420)
off-price retailer (412)	television home shopping (415)		transportation (420)
category killer (412)	online retailing (415)		carrier (420)
nonstore retailing (413)			

## Review Questions

1. In what ways is a channel of distribution different from the path taken by a product during physical distribution?
2. What are the most common marketing channels for consumer products? For industrial products?
3. What are the three general approaches to market coverage? What types of products is each approach used for?
4. What is a VMS? Identify examples of the three types of VMSs.
5. List the services performed by wholesalers. For whom is each service performed?
6. What is the basic difference between a merchant wholesaler and an agent?
7. Identify three kinds of full-service wholesalers. What factors are used to classify wholesalers into one of these categories?
8. Distinguish between (a) commission merchants and agents and (b) manufacturers' sales branches and manufacturers' sales offices.
9. What is the basic difference between wholesalers and retailers?
10. What is the difference between a department store and a discount store with regard to selling orientation and philosophy?
11. How do (a) convenience stores, (b) traditional specialty stores, and (c) category killers compete with other retail outlets?
12. What can nonstore retailers offer their customers that in-store retailers cannot?
13. Compare and contrast community shopping centers and regional shopping centers.
14. What is physical distribution? Which major functions does it include?
15. What activities besides storage are included in warehousing?
16. List the primary modes of transportation and cite at least one advantage of each.

## Discussion Questions

1. Which distribution channels would producers of services be most likely to use? Why?
2. Many producers sell to consumers both directly and through middlemen. How can such a producer justify competing with its own middlemen?
3. In what situations might a producer use agents or commission merchants rather than its own sales offices or branches?
4. If a middleman is eliminated from a marketing channel, under what conditions will costs decrease? Under what conditions will costs increase? Will the middleman's functions be eliminated? Explain.
5. Which types of retail outlets are best suited to intensive distribution? To selective distribution? To exclusive distribution? Explain your answer in each case.
6. How are the various physical distribution functions related to each other? To the other elements of the marketing mix?

## Video Case 14.1

### Taza Cultivates Channel Relationships with Chocolate

Taza Chocolate, a small Massachusetts-based manufacturer of stone-ground organic chocolate made in the classic Mexican tradition, sells most of its products to retailers, wholesalers, and distributors throughout the United States. Individual customers around the world can also buy Taza chocolate bars, baking squares, chocolate-covered nuts, and other specialty items

directly from Taza at the company's Web site, and if they live in Somerville (MA), they might even find a Taza employee riding a "chococycle," selling products and distributing samples at an upscale food truck festival or open market on a weekend.

With a staff of about 20 people, Taza sources all its ingredients directly from certified organic growers with whom

the company cultivates a personal relationship. “Because our process here at the factory is so minimal,” says the company’s director of sales, “it’s really important that we get a very high-quality ingredient. . . . The cocoa beans are the most important. . . . When we source those, we pay a premium above even fair trade prices. We call it direct trade. To make sure that we’re getting the absolute cream of the crop, we have a direct face-to-face human relationship between us and the actual farmer that’s producing those beans.”

The company believes that dealing directly with its suppliers is the best business model for Taza as a small firm not only because it allows the company to meet its social responsibility goals but also because it ensures quality, which commands a premium price. “We’re a premium brand,” says the director of sales, “and because of the way we do what we do, we have to charge more than your average chocolate bar. . . . There’s usually a 40 to 50 percent markup between wholesale sales and the price. . . . on the retail store shelf. So, say we sell a chocolate bar for \$4.50. . . . then the wholesale price is going to be somewhere around \$2.70 for that unit. . . . The distributor price [is] even lower, maybe around \$2.” Distributors buy in the largest quantities, which for Taza means a pallet load as opposed to a case that a wholesaler would buy. “But wholesale will always be our bread and butter, where we really move the volume and we have good margins. . . . It’s been challenging for us to work with distributors. They’re always squeezing you on price, or trying to give you charge backs, or run promotions or do sales. . . . whereas the average wholesale customer is, in our industry at least, . . . much more used to accepting what we give them in terms of promotions or pricing.”

Taza does almost no advertising, relying instead on Facebook, Twitter, a company blog, e-mail, and events that cre-

ate buzz like chocolate salons, food shows, in-store tastings, and especially frequent sampling in upscale and organic food stores in big metropolitan areas. The company tries to cultivate the same sort of personal relationships with members of its distribution channel as it does with its cocoa farmers. “When we send a shipment of chocolate,” says the sales director, “sometimes we’ll put in a little extra for the people who work there. That always helps because you’re building that kind of human relationship.”

A privately owned firm, Taza has just begun shipping its chocolate products internationally to Canada and a handful of European companies. Its marketing channel definitely plays a role in delivering products that are fresh. Shipping perishable products to customers in the summer, for instance, can be a problem. But “having a distributor. . . . that has a couple of thousand dollars of inventory in their refrigerated warehouse all the time changes that equation. It means the store can just order from that distributor, pay about the same price that they would pay if they ordered directly from us, [and] get the product probably the next day, with much lower shipping cost.”<sup>17</sup>

### Questions

1. Which distribution channels does Taza use?
2. In what ways does Taza benefit from selling directly to consumers? What are the potential problems that Taza may experience by selling directly to consumers?
3. If Taza wanted to grow its sales by broadening physical distribution of its products, do you think it should work more closely with its wholesalers or with its distributors? Why?

## Case 14.2

### Behind the Scenes at Costco



More than 20 years after Costco opened its first warehouse club store in Seattle, Washington, the company’s philosophy can still be summed up as “pile ‘em high, price ‘em low.” Costco stores are anything but fancy. In fact, the first store was located inside a warehouse. Yet 56 million consumers and small-business owners pay an annual membership fee so they can save on everything from mayonnaise, mattresses, and movies to laptops, lighting, and luggage. Each store (and the Costco retail Web site) carries a broad and varied merchandise assortment, all priced low to move quickly. In all, the retailer sells \$600 million worth of fine wines, \$1.4 billion worth of prescription medicines, 45 million hot dogs, and 60,000 carats of diamonds every year.

Customers never really know what products they will find each time they visit one of the 567 Costco warehouse stores around the world. Surprises are all part of the shopping experience at Costco. “The art form of our business is intuition,” says the CEO. His buyers must choose carefully, because the typical Costco carries less than 10 percent of the number of products displayed in a Walmart store.

Moreover, Costco aims for a profit margin of no more than 14 percent, which means inventory must sell quickly. If products sell slowly, they will tie up precious cash that could be better spent on newer or more popular merchandise. Therefore, Costco’s buyers watch for particularly hot products and product categories. Well-known manufacturers’ brands share shelf space with Kirkland Signature, Costco’s private brand. Members may walk past stacks of best-selling books on the right, color printers on the left, and racks of baked goods straight ahead as they push their shopping carts down the aisle. This variety enhances the store’s appeal, says the CEO: “Our customers do not drive 15 miles to save on a jar of peanut butter. They come for the treasure hunt.”

Among the treasures they might find: an \$8,000 Suzuki grand piano, a \$6,000 100-CD Wurlitzer jukebox, and a seven-carat diamond ring for \$125,000. Such items now comprise 5 to 10 percent of Costco’s sales. Despite the low prices, Costco offers a generous return policy. Customers can return anything at any time. If dissatisfied with their membership, they can even get a full refund on that.

The exception is electronic products, which cannot be brought back after 90 days. To help customers set up and use their new televisions, computers, and other electronics items, Costco offers free technical support by phone.

No receipt? No problem at Costco. Customers have ample opportunity to exchange or return items because they visit the stores frequently. Research shows that, on average, members visit Costco stores more than 11 times a year and spend \$94 on each visit. Each U.S. Costco store rings up, on average, \$139 million worth of merchandise annually, and its average sales per square foot is a whopping \$797. Costco's members are quite loyal, with a renewal rate of 86 percent, and they have a median income of \$72,000.

In recent years, Costco has continued its growth by offering new consumer and business services at low prices. For example, members can log on to the retailer's Web site (<http://www.costco.com>) and apply for a mortgage, buy life insurance, search for concert tickets, hire a Web site

designer, arrange for payroll service, or price a vacation trip. The company has also expanded its retail footprint, including opening new stores in urban areas such as New York City. Costco adapts its assortment for each store, based not only on the size of the warehouse but also on the needs of local shoppers. Downtown stores are typically smaller, because city locations are so costly, but every Costco store carries an ever-changing array of merchandise, reflecting the treasure hunt that brings customers back again and again in search of that next unexpected bargain.<sup>18</sup>

### Questions

1. How would you classify Costco as an in-store retailer? Why?
2. Evaluate Costco's objective of achieving a 14 percent profit margin. Explain your answer.
3. How do you think physical distribution affects Costco's ability to satisfy its customers?

## Building Skills for Career Success



### 1 JOURNALING FOR SUCCESS

**Discovery statement:** In this chapter, you learned that retailers are marketing intermediaries and part of the distribution channel.

#### Assignment

1. Thinking about brick-and-mortar retail stores, in which store have you had your most enjoyable shopping experience? Describe this retail store.
2. Discuss this shopping experience and why it was such a great shopping experience.
3. At what brick-and-mortar store did you have your worst experience? Describe this store.
4. Discuss this worst shopping experience and be sure to mention the reasons why this shopping experience was the worst one for you.

### 2 EXPLORING THE INTERNET

One reason the Internet has generated so much excitement and interest among both buyers and distributors of products is that it is a highly effective method of direct marketing.

Already a multibillion-dollar industry, e-commerce is growing as more businesses recognize the power of the Internet to reach customers 24 hours a day anywhere in the world. In addition to using the Internet to provide product information to potential customers, businesses can use it to process orders and accept payment from customers. Quick delivery from warehouses or stores by couriers such as UPS and FedEx adds to the convenience of Internet shopping.

Businesses whose products traditionally have sold well through catalogs are clear leaders in the electronic marketplace. Books, CDs, clothing, and other frequently purchased, relatively low-cost items sell well through both the Internet and catalogs. As a result, many successful catalog companies are including the Internet as a means of communicating about products. Many of their customers are finding that they prefer the more dynamic online versions of the catalogs.

#### Assignment

1. Explore the Web sites listed below, or just enter "shopping" on one of the Web search engines—then stand back! In addition, visit the text Web site for updates to this exercise.

<http://www.llbean.com>

<http://www.jcpenney.com>

<http://www.sears.com>

<http://www.landsend.com>

<http://www.barnesandnoble.com>

<http://www.amazon.com>

2. Which Web site does the best job of marketing merchandise? Explain your answer.
3. Find a product that you would be willing to buy over the Internet and explain why you would buy it. Name the Web site and describe the product.
4. Find a product that you would be unwilling to buy over the Internet and, again, explain your reasoning. Name the Web site and describe the product.

**3 DEVELOPING CRITICAL-THINKING SKILLS**

According to the wheel of retailing hypothesis, retail businesses begin as low-margin, low-priced, low-status operations. As they successfully challenge established retailers for market share, they upgrade their facilities and offer more services. This raises their costs and forces them to increase their prices so that eventually they become like the conventional retailers they replaced. As they move up from the low end of the wheel, new firms with lower costs and prices move in to take their place. For example, Kmart started as a low-priced operation that competed with department stores. Over time, it upgraded its facilities and products; big Kmart stores now offer such exclusive merchandise as Martha Stewart's bed-and-bath collection, full-service pharmacies, café areas, and "pantry" areas stocked with frequently bought grocery items, including milk, eggs, and bread. In consequence, Kmart has become a higher-cost, higher-priced operation and, as such, is vulnerable to lower-priced firms entering at the low end of the wheel.

**Assignment**

1. Investigate the operations of a local retailer.
2. Explain how this retailer is evolving on the wheel of retailing.
3. Prepare a report on your findings.

**4 BUILDING TEAM SKILLS**

Surveys are a commonly used tool in marketing research. The information they provide can reduce business risk and facilitate decision making. Retail outlets often survey their customers' wants and needs by distributing comment cards or questionnaires.

The customer survey below is an example of a survey that a local photography shop might distribute to its customers.

**Assignment**

1. Working in teams of three to five, choose a local retailer.
2. Classify the retailer according to the major types of retailers.
3. Design a survey to help the retailer to improve customer service. (You may find it beneficial to work with the retailer and actually administer the survey to the retailer's customers. Prepare a report of the survey results for the retailer.)
4. Present your findings to the class.

**5 RESEARCHING DIFFERENT CAREERS**

When you are looking for a job, the people closest to you can be extremely helpful. Family members and friends may be able to answer your questions directly or put you in touch with someone else who can. This type of "networking" can lead to an "informational interview," in which you can meet with someone who will answer your questions about a career or a company and who can also provide inside information on related fields and other helpful hints.

**Assignment**

1. Choose a retailer or wholesaler and a position within the company that interests you.
2. Call the company and ask to speak to the person in that particular position. Explain that you are a college student interested in the position, and ask to set up an "informational interview."
3. Prepare a list of questions to ask in the interview. The questions should focus on:
  - a. The type of training recommended for the position
  - b. How the person entered the position and advanced in it
  - c. What he or she likes and dislikes about the work
4. Present your findings to the class.

**CUSTOMER SURVEY**

To help us to serve you better, please take a few minutes while your photographs are being developed to answer the following questions. Your opinions are important to us.

1. Do you live/work in the area? (Circle one or both if they apply.)
2. Why did you choose us? (Circle all that apply.)
  - Close to home
  - Close to work
  - Convenience
  - Good service
  - Quality
  - Full-service photography shop
  - Other
3. How did you learn about us? (Circle one.)
  - Newspaper
  - Flyer/coupon
  - Passing by

Recommended by someone

Other

4. How frequently do you have film developed? (Please estimate.)
    - \_\_\_\_\_ Times per month
    - \_\_\_\_\_ Times per year
  5. Which aspects of our photography shop do you think need improvement?
  6. Our operating hours are from 8:00 a.m. to 7:00 p.m. weekdays and from 9:30 a.m. to 6:00 p.m. Saturdays. We are closed on Sundays and legal holidays. If changes in our operating hours would serve you better, please specify how you would like them changed.
  7. Age (Circle one.)
    - Under 25
    - 26–39
    - 40–59
    - Over 60
- Comments: