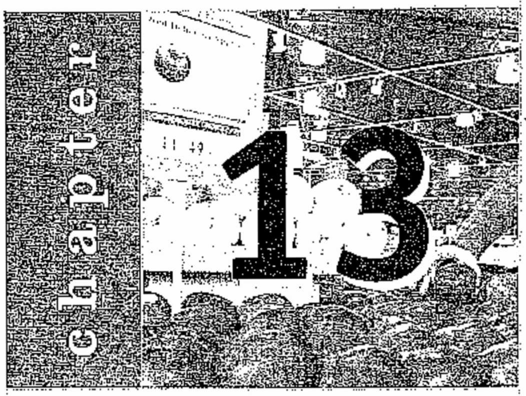


Retailing and Wholesaling

Previewing the Concepts

In the previous chapter, you learned the basics of distribution channel design and management. Now, we'll look more deeply into the two major intermediary channel functions, retailing and wholesaling. You already know something about retailing—you're served every day by retailers of all shapes and sizes. However, you probably know much less about the hoard of wholesalers that work behind the scenes. In this chapter, we'll examine the characteristics of different kinds of retailers and wholesalers, the marketing decisions they make, and trends for the future.

To start the tour, we'll look at Whole Foods Market. In today's marketing world, almost every retailer, large or small, worries about competing with Wal-Mart, the world's largest retailer—the world's second-largest *company*. Few retailers *can* compete directly with Wal-Mart and survive. Yet, little Whole Foods is thriving in the shadow of the giant.

These days, Wal-Mart sells just about everything. That means that it competes ruthlessly with almost every other retailer, no matter what the product category. Wal-Mart outsells Toys 'R' Us in the toy market and sells half again as many groceries as the leading groceries-only retailer, Kroger. It gives Blockbuster big headaches in DVD and video sales, and puts a big dent in Best Buy's consumer electronics business. Almost every retailer, large or small, has its hands full devising strategies by which it can compete with Wal-Mart and survive.

So, how *do* you compete with a behemoth like Wal-Mart? The best answer: You don't—at least not directly. Perhaps the worst strategy is trying to out-Wal-Mart Wal-Mart. Instead of competing head-to-head, smart competitors choose their turf carefully.

In fact, this story isn't even about Wal-Mart—we'll cover that colossus later in the chapter. Instead, this is a David-and-Goliath story about Whole Foods Market, a small, upscale grocery chain that's doing very well by carving out its own turf in the giant's shadow. Whole Foods has only 184 stores versus Wal-Mart's more than 6,500 worldwide, and its annual sales total about $4.7 billion, compared to Wal-Mart's $312 billion.

Although it may not seem like a fair fight, Whole Foods is thriving. It succeeds through careful positioning—specifically, by positioning *away* from Wal-Mart. Rather than pursuing mass-market sales volume and razor-thin margins, Whole Foods targets a select group of upscale customers and offers them "organic, natural, and gourmet foods, all swaddled in Earth Day politics." As one analyst puts it, "While other grocers are looking over their shoulder, watching and worrying about Wal-Mart, Whole Foods is going about business as usual. The tofu is still selling; the organic eggs are fresh in the back dairy cooler; and meats are still hormone free."

Whole Foods' value proposition is summed up in its motto: "Whole Foods, Whole People, Whole Planet."

> Counters groan with creamy hunks of artisanal cheese. Medjool dates beckon amid rows of exotic fruit. Savory breads rest near fruit-drenched pastries, and prepared dishes like sesame-encrusted tuna rival what's sold in fine restaurants. In keeping with the company's positioning, most of the store's goods carry labels proclaiming "organic," "100% natural," and "contains no additives." Staff people smile, happy to suggest wines that go with a particular cheese, or pause to debate the virtues of peanut butter maltballs. And it's all

done against a backdrop of eye-pleasing earth-toned hues and soft lighting. This is grocery shopping? Well, not as most people know it. Whole Foods Market has cultivated its mystique with shoppers . . . by being anything but a regular supermarket chain. Whole Foods is, well, special.

The Whole Foods Web site reinforces the company's positioning. The site offers up recipes for healthy eating, such as "Sweet Potato Pancakes with Creamy Dill Sauce," "Baked Basmati & Currant Stuffed Trout," and "Beginner's Tips for Tofu, Tempeh, and Other Soy Foods." The site bursts at the seams with information on a wide range of health and wellness issues, from sources such as the WholeHealthMD reference library and the American Botanical Council. You'll find all you ever wanted to know about topics ranging from the potential medical uses of over 100 herbs to alternative therapies such as acupuncture, reflexology, and homeopathy.

Both online and in the flesh, a visit to Whole Foods is more than just a shopping trip, it's an experience. And the experience is anything but what you'd find at Wal-Mart. "We create store environments that are inviting, fun, unique, informal, comfortable, attractive, nurturing, and educational," the company claims. "We want our stores to become community meeting places where our customers come to join their friends and to make new ones."

Objectives

After studying this chapter, you should be able to

1. explain the roles of retailers and wholesalers in the distribution channel
2. describe the major types of retailers and give examples of each
3. describe the major types of wholesalers and give examples of each
4. explain the marketing decisions facing retailers and wholesalers

By design, Whole Foods is not for everyone—the upscale retailer caters to a carefully selected segment of consumers. Whole Foods customers are affluent, liberal, educated people living in university towns such as Austin, Texas, Boulder, Colorado, and Ann Arbor, Michigan. Their median annual household income exceeds the U.S. average by almost $8,000. Whole Foods customers live a health-conscious lifestyle, care about the food they eat, and worry about the environment. They tend to be social do-gooders who abhor soulless corporate greed. Whole Foods doesn't really need to compete with mass merchandisers such as Wal-Mart for these customers. In fact, a Whole Foods customer is more likely to boycott the local Wal-Mart than to shop at it.

Whole Foods customers like the fact that the store's commitment to quality reaches far beyond what's on its shelves. In its "Declaration of Interdependence," the company recognizes that living up to its "Whole Foods, Whole People, Whole Planet" motto means doing more than simply selling food. It means caring about the well-being and quality of life of everyone associated with the business, from customers and employees, to suppliers, to the broader communities in which it operates.

Its concern for customers runs deep. "We go to extraordinary lengths to satisfy and delight our customers," says a company spokesperson. "We want to meet or exceed their expectations on every shopping trip." Whole Foods also cares about its employees—for the past nine years, it's been listed among *Fortune* magazine's "Top 100 Companies to Work for in America." Whole Foods cares about its suppliers. The Declaration of Interdependence states, "We view our trade partners as allies in serving our stakeholders. We treat them with respect, fairness, and integrity, and expect the same in return." To back this up, the company supports sustainable, environmentally friendly agriculture practices, offering organically grown foods almost exclusively.

Whole Foods also cares about its communities. It provides financial support for employees doing voluntary community service. And it invests in the local environment. One store in Berkeley, California, gets most of its electrical power from roof-top solar panels. A special electrical system and energy-conserving features make the most of the sun. Perhaps most telling of Whole Foods' broad community commitment: It donates 5 percent of its after-tax profits to not-for-profit organizations.

Such commitment, along with strong targeting and positioning, have made Whole Foods one of the nation's fastest growing and most profitable food retailers. It's now the world's number-one natural food chain. Its upscale stores ring up an average of $689 in sales per square foot, almost twice that of a traditional grocer. And the chain reaps 35 percent gross margins, half again as large as those of traditional competitors such as Kroger. Whereas other grocers have faced limited sales and profit growth or even declines in the face of the withering Wal-Mart assault, Whole Foods' sales and profits have doubled over the past four years.

So, Whole Foods can't compete directly with the Wal-Marts of the world. It can't match Wal-Mart's massive economies of scale, incredible volume purchasing power, ultraefficient logistics, wide selection, and hard-to-beat prices. But then again, it doesn't even try. Instead, it targets customers that Wal-Mart can't serve, offering them value that Wal-Mart can't deliver. By positioning away from Wal-Mart and other mainstream grocers, Whole Foods has found its own very profitable place in the world. Says Whole Foods chief executive, "Not everyone is concerned with getting mediocre food at the lowest price."[1]

The Whole Foods story sets the stage for examining the fast-changing world of today's resellers. This chapter looks at *retailing* and *wholesaling*. In the first section, we look at the nature and importance of retailing, major types of store and nonstore retailers, the decisions retailers make, and the future of retailing. In the second section, we discuss these same topics as they relate to wholesalers.

Retailing

Retailing
All activities involved in selling goods or services directly to final consumers for their personal, nonbusiness use.

Retailer
A business whose sales come *primarily* from retailing.

What is retailing? We all know that Wal-Mart, Home Depot, Macy's, and Target are retailers, but so are Avon representatives, Amazon.com, the local Hampton Inn, and a doctor seeing patients. **Retailing** includes all the activities involved in selling products or services directly to final consumers for their personal, nonbusiness use. Many institutions—manufacturers, wholesalers, and retailers—do retailing. But most retailing is done by **retailers**: businesses whose sales come *primarily* from retailing.

Although most retailing is done in retail stores, in recent years *nonstore retailing* has been growing much faster than has store retailing. Nonstore retailing includes selling to final consumers through direct mail, catalogs, telephone, the Internet, TV home-shopping shows, home and office parties, door-to-door contact, vending machines, and other direct-selling approaches. We discuss such direct-marketing approaches in detail in Chapter 17. In this chapter, we focus on store retailing.

Types of Retailers

Retail stores come in all shapes and sizes, and new retail types keep emerging. The most important types of retail stores are described in Table 13.1 and discussed in the following sections. They can be classified in terms of several characteristics, including the *amount of service* they offer, the breadth and depth of their *product lines*, the *relative prices* they charge, and how they are *organized*.

Amount of Service

Different products require different amounts of service, and customer service preferences vary. Retailers may offer one of three levels of service—self-service, limited service, and full service.

Self-service retailers serve customers who are willing to perform their own "locate-compare-select" process to save money. Self-service is the basis of all discount operations and

TABLE 13.1 Major Store Retailer Types

Specialty Stores: Carry a narrow product line with a deep assortment, such as apparel stores, sporting-goods stores, furniture stores, florists, and bookstores. A clothing store would be a *single-line* store, a men's clothing store would be a *limited-line store*, and a men's custom-shirt store would be a *superspecialty* store. Examples: Gap, The Athlete's Foot, Williams-Sonoma.
Department Stores: Carry several product lines—typically clothing, home furnishings, and household goods—with each line operated as a separate department managed by specialist buyers or merchandisers. Examples: Sears, Macy's, Neiman Marcus.
Supermarkets: A relatively large, low-cost, low-margin, high-volume, self-service operation designed to serve the consumer's total needs for grocery and household products. Examples: Safeway, Kroger, Albertsons, Publix.
Convenience Stores: Relatively small stores located near residential areas, open long hours seven days a week, and carrying a limited line of high-turnover convenience products at slightly higher prices. Examples: 7-Eleven, Stop-N-Go, Circle K.
Discount Stores: Carry standard merchandise sold at lower prices with lower margins and higher volumes. Examples: Wal-Mart, Target, Kohl's.
Off-Price Retailers: Sell merchandise bought at less-than-regular wholesale prices and sold at less than retail, often leftover goods, overruns, and irregulars obtained at reduced prices from manufacturers or other retailers. These include *factory outlets* owned and operated by manufacturers (example: Mikasa); *independent off-price retailers* owned and run by entrepreneurs or by divisions of larger retail corporations (example: TJ Maxx); and *warehouse (or wholesale) clubs* selling a limited selection of brand-name groceries, appliances, clothing, and other goods at deep discounts to consumers who pay membership fees (examples: Costco, Sam's, BJ's Wholesale Club).
Superstores: Very large stores traditionally aimed at meeting consumers' total needs for routinely purchased food and nonfood items. Includes *category killers*, which carry a deep assortment in a particular category and have a knowledgeable staff (examples: Best Buy, PetSmart, Staples); *supercenters*, combined supermarket and discount stores (examples: Wal-Mart Supercenters, SuperTarget, Super Kmart Center, Meijer); and *hypermarkets* with up to 220,000 square feet of space combining supermarket, discount, and warehouse retailing (examples: Carrefour [France], Pyrca [Spain]).

is typically used by sellers of convenience goods (such as supermarkets) and nationally branded, fast-moving shopping goods (such as Wal-Mart).

Limited-service retailers, such as Sears or JC Penney, provide more sales assistance because they carry more shopping goods about which customers need information. Their increased operating costs result in higher prices. In *full-service retailers*, such as specialty stores and first-class department stores, salespeople assist customers in every phase of the shopping process. Full-service stores usually carry more specialty goods for which customers like to be "waited on." They provide more services resulting in much higher operating costs, which are passed along to customers as higher prices.

Product Line

Specialty store
A retail store that carries a narrow product line with a deep assortment within that line.

Department store
A retail organization that carries a wide variety of product lines—each line is operated as a separate department managed by specialist buyers or merchandisers.

Supermarket
Large, low-cost, low-margin, high-volume, self-service store that carries a wide variety of grocery and household products.

Convenience store
A small store, located near a residential area, that is open long hours seven days a week and carries a limited line of high-turnover convenience goods.

Retailers also can be classified by the length and breadth of their product assortments. Some retailers, such as **specialty stores**, carry narrow product lines with deep assortments within those lines. Today, specialty stores are flourishing. The increasing use of market segmentation, market targeting, and product specialization has resulted in a greater need for stores that focus on specific products and segments.

In contrast, **department stores** carry a wide variety of product lines. In recent years, department stores have been squeezed between more focused and flexible specialty stores on the one hand, and more efficient, lower-priced discounters on the other. In response, many have added promotional pricing to meet the discount threat. Others have stepped up the use of store brands and single-brand "designer shops" to compete with specialty stores. Still others are trying mail-order, telephone, and Web selling. Service remains the key differentiating factor. Retailers such as Nordstrom, Saks, Neiman Marcus, and other high-end department stores are doing well by emphasizing high-quality service.

Supermarkets are the most frequently shopped type of retail store. Today, however, they are facing slow sales growth because of slower population growth and an increase in competition from discount food stores and supercenters on the one hand, and upscale specialty food stores on the other. Supermarkets also have been hit hard by the rapid growth of out-of-home eating. In fact, supermarkets' share of the groceries and consumables market plunged from 73 percent in 1998 to 51 percent in 2005.[2] Thus, many traditional supermarkets are facing hard times.

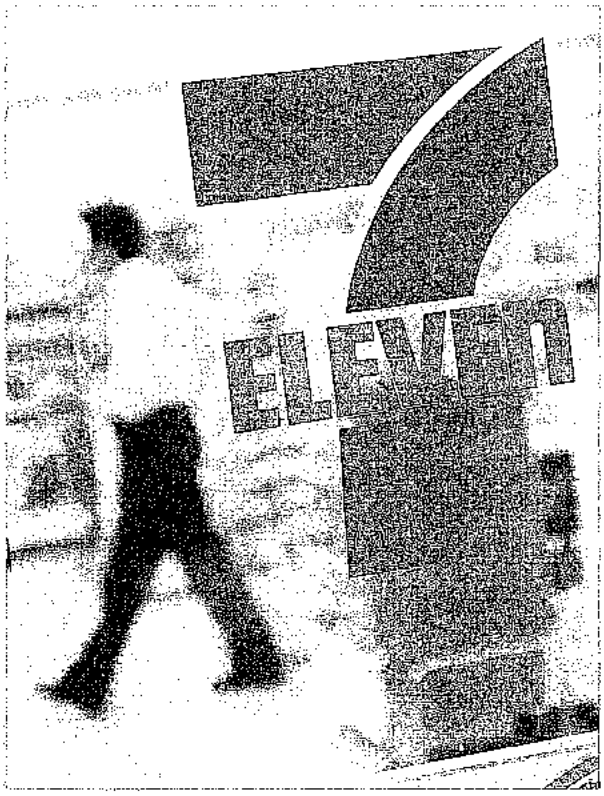
Many supermarkets are making improvements to attract more customers. In the battle for "share of stomachs," many large supermarkets are moving upscale, providing improved store environments and higher-quality food offerings, such as from-scratch bakeries, gourmet deli counters, and fresh seafood departments. For example, Safeway recently converted 300 of its stores to "lifestyle" formats, featuring subdued lighting, hardwood floors and display cabinets, and home departments. Others are cutting costs, establishing more efficient operations, and lowering prices in order to compete more effectively with food discounters. Finally, a few have added Web-based sales. Today, one-quarter of all grocery stores sell their goods online—including Safeway, Albertsons, D'Agostino, and others—the number is slowly growing. Forrester Research estimates that online grocery buying will grow to $17.4 billion by 2008.[3]

Convenience stores are small stores that carry a limited line of high-turnover convenience goods. After several years of stagnant sales, convenience stores are now experiencing healthy growth. Last year, U.S. convenience stores posted sales of $474 billion, a 20 percent increase over the previous year. More than 69 percent of convenience store revenues come

Facing increased competition, many supermarkets are providing improved store environments and higher quality food offerings. For example, Safeway recently converted 300 of its stores to "lifestyle" formats, featuring subdued lighting, hardwood floors and display cabinets, and home departments.

from sales of gasoline; a majority of in-store sales are from tobacco products (38 percent) and beer and other beverages (25 percent).[4]

In recent years, convenience store chains have tried to expand beyond their primary market of young, blue-collar men, redesigning their stores to attract female shoppers. They are shedding the image of a "truck stop" where men go to buy beer, cigarettes, and magazines, and instead offer fresh prepared foods and cleaner, safer, more upscale environments. Consider this example:[5]



Convenience store makeover: 7-Eleven is shedding its "truck stop" image and transforming its stores to offer more upscale assortments and environments.

> There's something familiar about the place, with its muted orange-and-green color scheme. The aisles are wider, though, and the displays tonier. Chilling in the fridge is the house Chardonnay, not far from a glass case packed with baguettes and cream cheese croissants that come piping-hot out of the onsite oven. An aisle away is the snazzy cappuccino machine, which offers up bananas foster and pumpkin spice java. There's sushi and, of course, bouquets of fresh-cut flowers. They're right next to the Slurpee machine. Yes, this decidedly upscale little shoppe is a 7-Eleven—or it will be, once the company's team of ace technologists, trendspotters, and product developers wrap up one of the most ambitious makeovers in business history.
>
> The convenience king, most commonly known for lowbrow though popular features such as the Big Gulp and around-the-clock access to Twinkies, is moving up the food chain in search of more affluent customers and fatter margins. After all, the majority of convenience store sales come from gasoline and cigarettes—two increasingly stagnant categories. So 7-Eleven is banking on a new, inventive inventory mix that competes more with Starbucks than with Shell. The transformation seems to be working. After declaring bankruptcy in 1990, the company's fortunes turned around last year. Sales were up 12 percent; profits jumped 66 percent.

Superstore
A store much larger than a regular supermarket that offers a large assortment of routinely purchased food products, nonfood items, and services.

Category killer
Giant specialty store that carries a very deep assortment of a particular line and is staffed by knowledgeable employees.

Superstores are much larger than regular supermarkets and offer a large assortment of routinely purchased food products, nonfood items, and services. Wal-Mart, Target, Meijer, and other discount retailers offer *supercenters*, very large combination food and discount stores. Supercenters are growing in the United States at an annual rate of 25 percent, compared with a supermarket industry growth rate of only 1 percent. Wal-Mart, which opened its first supercenter in 1988, now has almost 2,000 worldwide, capturing more than 70 percent of all supercenter volume.[6]

Recent years have also seen the explosive growth of superstores that are actually giant specialty stores, the so-called **category killers**. They feature stores the size of airplane hangars that carry a very deep assortment of a particular line with a knowledgeable staff. Category killers are prevalent in a wide range of categories, including books, baby gear, toys, electronics, home-improvement products, linens and towels, party goods, sporting goods, even pet supplies. Another superstore variation, a *hypermarket*, is a huge superstore, perhaps as large as *six* football fields. Although hypermarkets have been very successful in Europe and other world markets, they have met with little success in the United States.

Finally, for some retailers, the product line is actually a service. Service retailers include hotels and motels, banks, airlines, colleges, hospitals, movie theaters, tennis clubs, bowling alleys, restaurants, repair services, hair salons, and dry cleaners. Service retailers in the United States are growing faster than product retailers.

Relative Prices

Retailers can also be classified according to the prices they charge (see Table 13.1). Most retailers charge regular prices and offer normal-quality goods and customer service. Others

Real Marketing

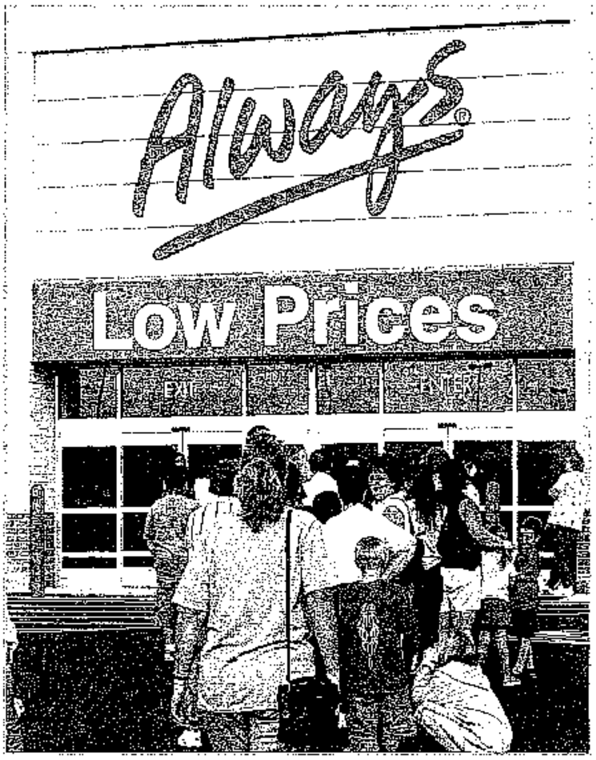
13.1 Wal-Mart is the world's largest retailer, and it's playing tag-team with ExxonMobil for the title of world's largest *company*. Wal-Mart is almost unimaginably big. It rang up an incredible $316 billion in sales last year—that's 1.7 times the sales of competitors Costco, Target, Sears/Kmart, JC Penney, and Kohl's *combined*.

Wal-Mart is the number-one seller in several categories of consumer products, including groceries, toys, CDs, and pet-care products. It sells more clothes than the Gap and Limited combined and almost twice as many groceries as Kroger, the leading grocery-only food retailer. Incredibly, Wal-Mart sells 30 percent of the disposable diapers purchased in the United States each year, 30 percent of the hair-care products, 26 percent of the toothpaste, and 20 percent of the pet food. On average, some 130 million people visit Wal-Mart stores each week.

It's also hard to fathom Wal-Mart's impact on the U.S. economy. It's the nation's largest employer—one out of every 230 men, women, and children in the United States is a Wal-Mart associate. Its sales of $1.52 billion on one day in 2003 exceeded the GDPs of 26 countries. According to one study, Wal-Mart was responsible for some 25 percent of the nation's astonishing productivity gains during the 1990s. Another study found that—through its own low prices and through its impact on competitors' prices—Wal-Mart saved the American public $263 billion in 2004 alone—or $2,329 per household.

What are the secrets behind this spectacular success? First and foremost, Wal-Mart is passionately dedicated to its winning value proposition of "Always Low Prices, *Always!*" Its mission is to "lower the world's cost of living." To accomplish this mission, Wal-Mart offers a broad selection of carefully selected goods at unbeatable prices. No other retailer has come nearly so close to mastering the concepts of everyday low prices and one-stop shopping. As one analyst puts it, "The company gospel . . . is relatively simple: Be an agent for customers—find out what they want, and sell it to them for the lowest possible price." Says Wal-Mart's president and chief executive, "We're obsessed with delivering value to customers."

How does Wal-Mart make money with such low prices? The answer is deceptively simple. Wal-Mart is a lean, mean, distribution machine—it has the lowest cost structure in the industry. Low costs let the giant retailer charge lower prices but still reap higher profits. For example, grocery prices drop an average of 10 to 15 percent in



Leading discounters, such as Wal-Mart, now dominate the retail scene. First and foremost, Wal-Mart is passionately dedicated to its value proposition of "Always Low Prices, Always!"

offer higher-quality goods and service at higher prices. The retailers that feature low prices are discount stores and "off-price" retailers.

Discount store
A retail operation that sells standard merchandise at lower prices by accepting lower margins and selling at higher volume.

Off-price retailer
Retailer that buys at less-than-regular wholesale prices and sells at less than retail. Examples are factory outlets, independents, and warehouse clubs.

A **discount store** sells standard merchandise at lower prices by accepting lower margins and selling higher volume. The early discount stores cut expenses by offering few services and operating in warehouselike facilities in low-rent, heavily traveled districts. Today's discounters have improved their store environments and increased their services, while at the same time keeping prices low through lean, efficient operations. Leading discounters, such as Wal-Mart, now dominate the retail scene (see Real Marketing 13.1).

As the major discount stores traded up, a new wave of **off-price retailers** moved in to fill the ultralow-price, high-volume gap. Ordinary discounters buy at regular wholesale prices and accept lower margins to keep prices down. In contrast, off-price retailers buy at less-than-regular wholesale prices and charge consumers less than retail. Off-price retailers can be found in all areas, from food, clothing, and electronics to no-frills banking and discount brokerages.

markets Wal-Mart has entered, and Wal-Mart's food prices average 20 percent less than its grocery store rivals. Lower prices attract more shoppers, producing more sales, making the company more efficient, and enabling it to lower prices even more.

Wal-Mart's low costs result in part from superior management and sophisticated technology. Its Bentonville, Arkansas, headquarters contains a computer communications system that the U.S. Defense Department would envy, giving managers around the country instant access to sales and operating information. And its huge, fully automated distribution centers employ the latest technology to supply stores efficiently.

Wal-Mart also keeps costs down through good old "tough buying." The company is known for the calculated way it wrings low prices from suppliers. "Don't expect a greeter and don't expect friendly," says one supplier's sales executive after a visit to Wal-Mart's buying offices. "Once you are ushered into one of the spartan little buyers' rooms, expect a steely eye across the table and be prepared to cut your price. They are very, very focused people, and they use their buying power more forcefully than anyone else in America."

Some critics argue that Wal-Mart squeezes its suppliers too hard, driving some out of business. Wal-Mart proponents counter, however, that it is simply acting in its customers' interests by forcing suppliers to be more efficient. "Wal-Mart is tough, but totally honest and straightforward in its dealings with vendors," says an industry consultant. "Wal-Mart has forced manufacturers to get their act together."

Despite its incredible success over the past four decades, some analysts see chinks in the seemingly invincible Wal-Mart's armor. For example, its same-store sales are growing at a slower clip than those of Target and other spryer competitors, causing Wal-Mart's stock to languish. And to many higher-income consumers, Wal-Mart seems downright dowdy compared with the younger, hipper Target. "Many of its upscale customers . . . come into the store for vegetables, cereal, detergent, and the like—but turn up their noses at higher margin items such as apparel and electronics," says an analyst.

So, to reignite growth and to extend its customer base by capturing a larger share-of-wallet from higher-income consumers, Wal-Mart recently began giving itself a modest image facelift. It's sprucing up its stores and adding new, higher-quality merchandise. For example, many urban Wal-Marts now carry a slew of higher-end consumer electronics products, from Sony plasma televisions to Toshiba laptops to Apple iPods. And it's now dressing up its apparel racks with more stylish fashion lines under brand names such as Metro 7 and George by designer Mark Eisen.

Wal-Mart is also beefing up its spending on more stylish advertising. Gone are the old bouncing smiley-face, "roll back the prices" ads. In their place are ads that look more like, well, Target ads. Maybe that's because Wal-Mart's new chief marketing executive—and the architect of the image makeover—is a 20-year Target marketing veteran.

Even with its slightly more upscale image, however, in no way will Wal-Mart ever give up its core "Always Low Prices—*Always*" value proposition. After all, it is and always will be a discount store. And despite some growing pains, Wal-Mart appears well on its way to becoming the world's first trillion-dollar corporation. This leads some observers to wonder if an ever-larger Wal-Mart can retain its customer focus and positioning. The company's managers are betting on it. No matter where it operates, Wal-Mart's announced policy is to take care of customers "one store at a time." Says one top executive: "We'll be fine as long as we never lose our responsiveness to the consumer."

Sources: Quotes and other information from Bill Saporito and Jerry Useem, "One Nation Under Wal-Mart," *Fortune*, March 3, 2003, pp. 65–78; Don Longo, "Wal-Mart on Its Way to Becoming the First Trillion Dollar Corporation," *Retail Merchandiser*, March 2005, p. 7; Pallavi Gogoi, "Wal-Mart Gets the Fashion Bug," *BusinessWeek Online*, October 7, 2006, accessed at www.businessweek.com; Luke Boggs, "Why I'm Fighting for Wal-Mart," *DSN Retailing Today*, December 19, 2005, p. 11; "The Fortune 500," *Fortune*, April 17, 2006, pp. F1-F3; Theresa Howard, "Ads Try to Expand Customer Base," *USA Today*, February 21, 2006; Stuart Elliot and Michael Barbaro, "Wal-Mart on the Hunt for an Extreme Makeover," May 4, 2006, pp. C1, C13; Robert Berner, "Fashion Emergency at Wal-Mart," *BusinessWeek*, July 31, 2006, p. 67; and www.walmartstores.com January 2007.

Independent off-price retailer
Off-price retailer that is either owned and run by entrepreneurs or is a division of a larger retail corporation.

Factory outlet
Off-price retailing operation that is owned and operated by a manufacturer and that normally carries the manufacturer's surplus, discontinued, or irregular goods.

The three main types of off-price retailers are *independents*, *factory outlets*, and *warehouse clubs*. **Independent off-price retailers** either are owned and run by entrepreneurs or are divisions of larger retail corporations. Although many off-price operations are run by smaller independents, most large off-price retailer operations are owned by bigger retail chains. Examples include store retailers such as TJ Maxx and Marshall's, owned by TJX Companies, and Web sellers such as Overstock.com.

Factory outlets—producer-operated stores by firms such as Liz Claiborne, Carters, Levi Strauss, and others—sometimes group together in *factory outlet malls* and *value-retail centers*, where dozens of outlet stores offer prices as low as 50 percent below retail on a wide range of items. Whereas outlet malls consist primarily of manufacturers' outlets, value-retail centers combine manufacturers' outlets with off-price retail stores and department store clearance outlets, such as Nordstom Rack, Neiman Marcus Last Call Clearance Centers, and Off 5th (Saks Fifth Avenue outlets). Factory outlet malls have become one of the hottest growth areas in retailing.

The malls now are moving upscale—and even dropping "factory" from their descriptions—narrowing the gap between factory outlet and more traditional forms of retailers. As the gap narrows, the discounts offered by outlets are getting smaller. However, a growing number of outlet malls now feature brands such as Coach, Polo, Ralph Lauren, Dolce & Gabbana, Giorgio Armani, Gucci, and Versace, causing department stores to protest to the manufacturers of these brands. Given their higher costs, the department stores must charge more than the off-price outlets. Manufacturers counter that they send last year's merchandise and seconds to the factory outlet malls, not the new merchandise that they supply to the department stores. Still, the department stores are concerned about the growing number of shoppers willing to make weekend trips to stock up on branded merchandise at substantial savings.

Warehouse club
Off-price retailer that sells a limited selection of brand name grocery items, appliances, clothing, and a hodgepodge of other goods at deep discounts to members who pay annual membership fees.

Warehouse clubs (or *wholesale clubs* or *membership warehouses*), such as Sam's Club, Costco, and BJ's, operate in huge, drafty, warehouselike facilities and offer few frills. Customers themselves must wrestle furniture, heavy appliances, and other large items to the checkout line. Such clubs make no home deliveries and often accept no credit cards. However, they do offer ultralow prices and surprise deals on selected branded merchandise.

Although they account for only about 8 percent of total U.S. retail sales, warehouse clubs have grown rapidly in recent years. These retailers appeal not just to low-income consumers seeking bargains on bare-bones products; they appeal to all kinds of customers shopping for a wide range of goods, from necessities to extravagances. Consider Costco, the nation's largest warehouse retailer:

> What Costco has come to stand for is a retail segment where high-end products meet deep-discount prices. It's the U.S.'s biggest seller of fine wines (including the likes of a Chateau Cheval-Blanc Bordeaux for $229.99 a bottle) and baster of poultry (55,000 rotisserie chickens a day). Last year it sold 45 million hot dogs at $1.50 each and 60,000 carats of diamonds at up to $100,000. It even offered a Pablo Picasso drawing at Costco.com for only $129,999.99! Yuppies seek the latest gadgets there. Even people who don't have to pinch pennies shop at Costco.
>
> There was a time when only the great unwashed shopped at off-price stores. But warehouse clubs attract a breed of urban sophisticates attuned to what one retail consultant calls the "new luxury." These shoppers shun Seiko watches for TAG Heuer; Jack Nicklaus golf clubs for Callaway; Maxwell House coffee (it goes without saying) for Starbucks. They "trade up," eagerly spending more for items that make their hearts pound and for which they don't have to pay full price. Then they "trade down" to private labels for things like paper towels, detergent, and vitamins. Catering to this fast-growing segment, Costco has exploded too. "It's the ultimate concept in trading up and trading down," says the consultant. "It's a brilliant innovation for the new luxury."[7]

Off-price retailers: Shoppers at warehouse clubs such as Costco "trade down" to private labels for things like paper towels, detergent, and vitamins. At the same time, they "trade up," getting good prices on items that make their hearts pound. Costco even offered a Pablo Picasso drawing at its Web site—for only $129,999.99.

Organizational Approach

Although many retail stores are independently owned, others band together under some form of corporate or contractual organization. The major types of retail organizations—*corporate chains*, *voluntary chains* and *retailer cooperatives*, *franchise organizations*, and *merchandising conglomerates*—are described in Table 13.2.

Chain stores
Two or more outlets that are commonly owned and controlled.

Chain stores are two or more outlets that are commonly owned and controlled. They have many advantages over independents. Their size allows them to buy in large quantities at lower prices and gain promotional economies. They can hire specialists to deal with areas such as pricing, promotion, merchandising, inventory control, and sales forecasting.

The great success of corporate chains caused many independents to band together in one of two forms of contractual associations. One is the *voluntary chain*—a wholesaler-sponsored

TABLE 13.2 Major Types of Retail Organizations

Type	Description	Examples
Corporate chain stores	Two or more outlets that are commonly owned and controlled, employ central buying and merchandising, and sell similar lines of merchandise. Corporate chains appear in all types of retailing, but they are strongest in department stores, food stores, drug stores, shoe stores, and women's clothing stores.	Sears, Safeway (grocery stores), CVS (drug stores), Williams-Sonoma (cookware, dinnerware, and housewares)
Voluntary chains	Wholesaler-sponsored groups of independent retailers engaged in bulk buying and common merchandising.	Independent Grocers Alliance (IGA), Do-It Best hardwares, Western Auto, True Value
Retailer cooperatives	Groups of independent retailers who set up a central buying organization and conduct joint promotion efforts.	Associated Grocers (groceries), Ace (hardware)
Franchise organizations	Contractual association between a franchiser (a manufacturer, wholesaler, or service organization) and franchisees (independent businesspeople who buy the right to own and operate one or more units in the franchise system). Franchise organizations are normally based on some unique product, service, or method of doing business, or on a trade name or patent, or on goodwill that the franchiser had developed.	McDonald's, Subway, Pizza Hut, Jiffy Lube, Meineke Mufflers, 7-Eleven
Merchandising conglomerates	Free-form corporations that combine several diversified conglomerates retailing lines and forms under central ownership, along with some integration of their distribution and management functions.	Limited Brands

group of independent retailers that engages in group buying and common merchandising—which we discussed in Chapter 12. Examples include Independent Grocers Alliance (IGA), Western Auto, and Do-It Best hardware. The other type of contractual association is the *retailer cooperative*—a group of independent retailers that bands together to set up a jointly owned, central wholesale operation and conducts joint merchandising and promotion efforts. Examples are Associated Grocers and Ace Hardware. These organizations give independents the buying and promotion economies they need to meet the prices of corporate chains.

Franchise
A contractual association between a manufacturer, wholesaler, or service organization (a franchiser) and independent businesspeople (franchisees) who buy the right to own and operate one or more units in the franchise system.

Another form of contractual retail organization is a **franchise**. The main difference between franchise organizations and other contractual systems (voluntary chains and retail cooperatives) is that franchise systems are normally based on some unique product or service; on a method of doing business; or on the trade name, goodwill, or patent that the franchiser has developed. Franchising has been prominent in fast foods, health and fitness centers, haircutting, auto rentals, motels, travel agencies, real estate, and dozens of other product and service areas.

But franchising covers a lot more than just burger joints and fitness centers. Franchises have sprung up to meet about any need. Franchiser Mad Science Group franchisees put on science programs for schools, scout troops, and birthday parties. Mr. Handyman provides repair services for homeowners, and Merry Maids tidies up their houses.

Once considered upstarts among independent businesses, franchises now command 40 percent of all retail sales in the United States. These days, it's nearly impossible to stroll down a city block or drive on a suburban street without seeing a McDonald's, Subway, Jiffy Lube, or Holiday Inn. One of the best-known and most successful franchisers, McDonald's, now has nearly 32,000 stores in 119 countries. It serves nearly 50 million customers a day and racks up more than $39 billion in annual systemwide sales. Some 58 percent of McDonald's restaurants worldwide are owned and operated by franchisees. Gaining fast is Subway Sandwiches and Salads, one of the fastest-growing franchises, with more than 26,000 shops in 85 countries, including over 20,000 in the United States.[8]

Finally, *merchandising conglomerates* are corporations that combine several different retailing forms under central ownership. An example is Limited Brands, which operates The Limited (fashion-forward women's clothing), Express (trendy private-label women's and men's apparel), Victoria's Secret (glamorous lingerie and beauty products), Bath & Body

Franchising: These days, it's nearly impossible to stroll down a city block or drive on a suburban street without seeing a McDonald's, Jiffy Lube, Subway, or Holiday Inn.

Works (natural but luxurious beauty and body-care products), and The White Barn Candle Company (home fragrance and décor items). Such diversified retailing, similar to a multi-branding strategy, provides superior management systems and economies that benefit all the separate retail operations.

Retailer Marketing Decisions

Retailers are always searching for new marketing strategies to attract and hold customers. In the past, retailers attracted customers with unique product assortments and more or better services. Today, retail assortments and services are looking more and more alike. National-brand manufacturers, in their drive for volume, have placed their branded goods everywhere. Such brands are found not only in department stores but also in mass-merchandise discount stores, off-price discount stores, and on the Web. Thus, it's now more difficult for any one retailer to offer exclusive merchandise.

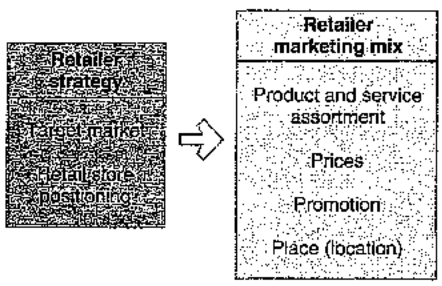
Service differentiation among retailers has also eroded. Many department stores have trimmed their services, whereas discounters have increased theirs. Customers have become smarter and more price sensitive. They see no reason to pay more for identical brands, especially when service differences are shrinking. For all these reasons, many retailers today are rethinking their marketing strategies.

As shown in Figure 13.1, retailers face major marketing decisions about their *target market* and *positioning*, *product assortment and services*, *price*, *promotion*, and *place*.

Target Market and Positioning Decision

Retailers must first define their target markets and then decide how they will position themselves in these markets. Should the store focus on upscale, midscale, or downscale shoppers? Do target shoppers want variety, depth of assortment, convenience, or low prices? Until they define and profile their markets, retailers cannot make consistent decisions about product assortment, services, pricing, advertising, store décor, or any of the other decisions that must support their positions.

FIGURE 13.1
Retailer marketing decisions

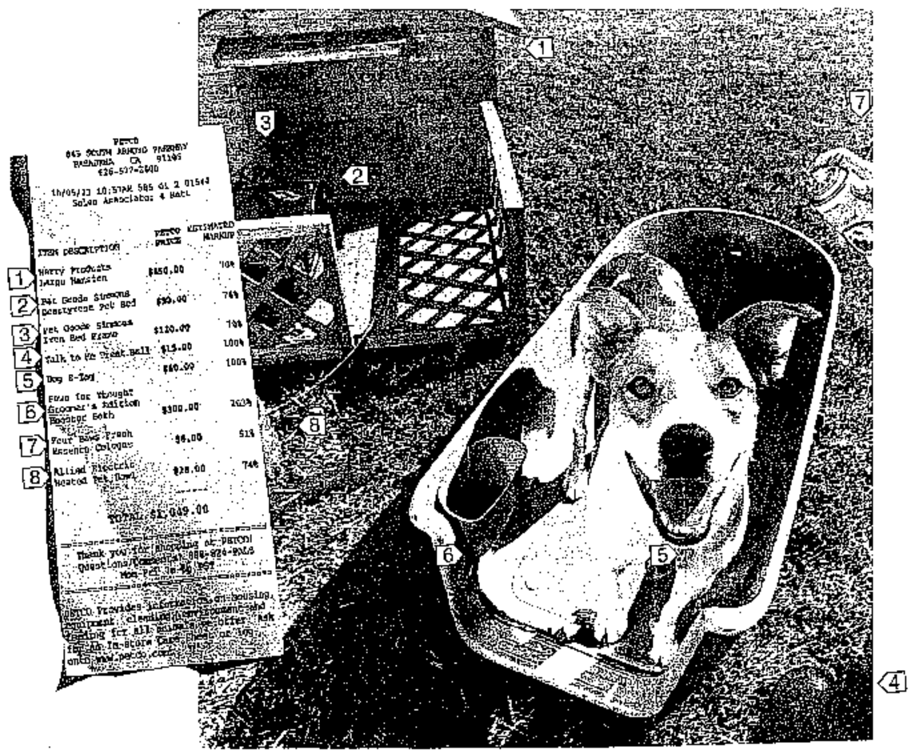


Too many retailers fail to define their target markets and positions clearly. They try to have "something for everyone" and end up satisfying no market well. In contrast, successful retailers define their target markets well and position themselves strongly. For example, Wal-Mart positions itself strongly on low prices. In a recent survey testing consumers on their recall of the slogans for American brands, 67 percent of consumers associated Wal-Mart with its "Always low prices. *Always*" promise. Sprite, in second place, scored just 35 percent recognition.[9]

If Wal-Mart owns the low-price position, how can other discounters hope to compete? Again, the answer is good targeting and positioning. For example, rather than facing Wal-Mart head-on, Target—or Tar-*zhay* as many fans call it—thrives by aiming at a seemingly oxymoronic "upscale discount" niche. It has become the nation's number-two discount chain by offering discount prices but rising above the discount fray with upmarket style and design and higher-grade service. Target's "expect more, pay less" positioning sets it apart and helps insulate it from Wal-Mart.

In the same way, pet-supply chain Petco competes effectively with low-priced competitors Wal-Mart and PetSmart by positioning upscale:

> With Gen Xers postponing child rearing and baby boomers coping with empty nests, more Americans are treating pets like spoiled kids with fur. "The way people view animals in the household has changed dramatically" in recent years, says a Petco executive, noting that 55 percent of pet canines now sleep in their owners' beds. People are now spending "more on what could be considered frivolous products," adds an industry consultant, "such as things to coddle their pets."
>
> This trend has been a boon for pets everywhere, but Sparky's not the only one wagging his tail. It's also been good for Petco. Ten years ago Petco made most of its money selling food. Today two-thirds of its revenue comes from services like grooming and training, and from specialty goods like $7.50 beef-flavored toothpaste and $30 pheromone-emitting stress reducers. This shift to pricier offerings has helped Petco avoid a catfight with Wal-Mart, a growing pet-supply power. Of Petco's 10,000 offerings, only 40 overlap with Wal-Mart's. And going upscale has given Petco higher operating margins than the more warehouse-focused PetSmart, the industry's top dog. Such smart targeting and positioning have earned Petco more than 12 consecutive years of double-digit income growth.[10]



Retail positioning: To avoid dog-eat-dog competition with Wal-Mart and cost-focused market leader PetSmart, Petco has transformed itself into an emporium of luxury pet supplies.

Product Assortment and Services Decision

Retailers must decide on three major product variables: *product assortment*, *services mix*, and *store atmosphere*.

The retailer's *product assortment* should differentiate the retailer while matching target shoppers' expectations. One strategy is to offer merchandise that no other competitor carries, such as private brands or national brands on which it holds exclusives. For example, Saks gets exclusive rights to carry a well-known designer's labels. It also offers its own private-label lines—the Saks Fifth Avenue Signature, Classic, and Sport collections. At JC Penney, private-label brands account for 40 percent of sales.[11]

Another strategy is to feature blockbuster merchandising events—Bloomingdale's is known for running spectacular shows featuring goods from a certain country, such as India or China. Or the retailer can offer surprise merchandise, as when Costco offers surprise assortments of seconds, overstocks, and closeouts. Finally, the retailer can differentiate itself by offering a highly targeted product assortment—Lane Bryant carries plus-size clothing; Brookstone offers an unusual assortment of gadgets in what amounts to an adult toy store.

The *services mix* can also help set one retailer apart from another. For example, some retailers invite customers to ask questions or consult service representatives in person or via phone or keyboard. Home Depot offers a diverse mix of services to do-it-yourselfers, from "how-to" classes to a proprietary credit card. Nordstrom promises to "take care of the customer, no matter what it takes."

The *store's atmosphere* is another element in the reseller's product arsenal. Every store has a physical layout that makes moving around in it either hard or easy. Each store has a "feel"; one store is cluttered, another cheerful, a third plush, a fourth somber. The retailer must design an atmosphere that suits the target market and moves customers to buy. For example, Apple's retail stores are very seductive places. They're what one analyst calls "a Space-Age vision of a Kubrickian future—full of gleaming white and dull silver hardware."[12] The store design is clean, simple, and just oozing with style—much like an Apple iPod or Mac PC. Shoppers are invited to stay a while, use the equipment, and soak up all of the exciting new technology. One shopper sums up the Apple store atmosphere and experience this way:

> It has become something of a second home to me—or, as I jokingly call it, "my temple." I've been known to spend hours at a time there. It seems a trifling thing that I can walk up to any terminal in the place during a . . . shopping break, log in to my e-mail account, and attend to my electronic correspondence. I am also able to freely Web-surf, instant-message, or do a bit of e-shopping (heck, even buy a new Mac or iPod on the online Apple Store). No one rushes or hassles me. It seems like a family room (albeit a gigantic one), with its comfortable theater seating in the back, its library-style shelves lined neatly with Mac software, books and magazines, its rows of flat-panel screens flashing Pixar trailers, its speaker-connected iPods cranking out catchy tunes, its low-to-the-ground kids' table and ball-shaped chairs for iMac gaming, and its Genius Bar, to which visitors could cozy up for guidance or troubleshooting with an Apple supergeek. That's why I sometimes don't want to leave. In fact, I wrote part of this essay on a MacBook laptop while reclining in one of those airport-style chairs. It's a testament to Apple retail savvy that I felt totally at ease while typing away.[13]

Store atmosphere: Apple's retail stores are very seductive places. Here, people wait in line to enter the new Apple store on Fifth Avenue in New York City. "It has become something of a second home to me," says one shopper, "or, as I jokingly call it, 'my temple'."

It's no wonder that Apple stores "are going gangbusters," says the analyst. "The stores are attracting up to 10,000 visitors per week each, or 18.1 million visitors a year in total." By comparison, Gateway's more pedestrian retail stores pulled in an average of only 250 people a week.

Other retailers practice "experiential retailing." At an REI store, consumers can try out climbing equipment on a huge wall in the store, or they can test Gore-Tex raincoats by going under a simulated rain shower. At Lifestyles Spa in Van Nuys, California, shoppers are invited to wear their bathing suits to the store and slip into water-filled Jacuzzis and hot tubs for a "test drive." Similarly, Maytag has set up "try-before-you-buy" stores in which it displays products in realistic home kitchen and laundry room settings, beckoning customers to try out products before making a choice. They can do a load of laundry, bake a sheet of cookies, or listen to a dishwasher to see whether it's really quiet.[14]

Increasingly, retailers are turning their stores into theaters that transport customers into unusual, exciting shopping environments. For example, outdoor goods retailer Cabela's stores are as much natural history museums for outdoor enthusiasts as they are retail outlets (see Real Marketing 13.2). And the huge Mall of America near Minneapolis is a veritable playground that attracts as many as 42 million visitors each year. Under a single roof, it shelters more than 520 specialty stores, some 50 restaurants, a wedding chapel that has married over 4,000 couples, a college campus, an enormous LEGO Imagination Center, an ice-skating rink, an aquarium, a two-story miniature golf course, and Underwater Adventures, which features hundreds of marine specimens and a dolphin show. Shoppers who wear themselves out can visit the new nap store, which features walls thick enough to shut out the sounds of screaming kids or the amusement park attractions. It sells shut-eye for 70 cents a minute.[15]

All of this confirms that retail stores are much more than simply assortments of goods. They are environments to be experienced by the people who shop in them. Store atmospheres offer a powerful tool by which retailers can differentiate their stores from those of competitors.

Price Decision

A retailer's price policy must fit its target market and positioning, product and service assortment, and competition. All retailers would like to charge high markups and achieve high volume, but the two seldom go together. Most retailers seek *either* high markups on lower volume (most specialty stores) *or* low markups on higher volume (mass merchandisers and discount stores).

Thus, Bijan's boutique with locations in New York City and on Rodeo Drive in Beverly Hills sells "the most expensive menswear in the world." Its million-dollar wardrobes include \$50 socks, \$375 silk ties, and \$19,000 ostrich-skin vests. Its "by appointment only" policy is designed to make its wealthy, high-profile clients comfortable with these prices. Says Mr. Bijan, "If a man is going to spend \$400,000 on his visit, don't you think it's only fair that he have my full attention?"[16] Bijan's sells a low volume but makes hefty profits on each sale. At the other extreme, TJ Maxx sells brand-name clothing at discount prices, settling for a lower margin on each sale but selling at a much higher volume.

Retailers must also decide on the extent to which they will use sales and other price promotions. Some retailers use no price promotions at all, competing instead on product and service quality rather than on price. For example, it's difficult to imagine Bijan's holding a two-for-the-price-of-one sale. Other retailers practice *"high-low" pricing*—charging higher prices on an everyday basis, coupled with frequent sales and other price promotions to increase store traffic, clear out unsold merchandise, create a low-price image, or attract customers who will buy other goods at full prices. Still others—such as Wal-Mart, Costco, Home Depot, and other mass retailers—practice *everyday low pricing (EDLP)*, charging constant, everyday low prices with few sales or discounts. Which strategy is best depends on the retailer's marketing strategy and the pricing approaches of competitors.[17]

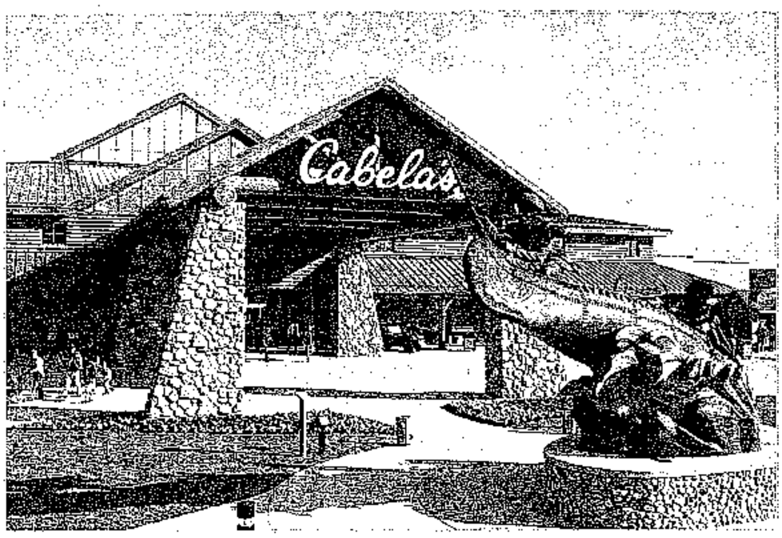
Promotion Decision

Retailers use any or all of the promotion tools—advertising, personal selling, sales promotion, public relations, and direct marketing—to reach consumers. They advertise in newspapers, magazines, radio, television, and on the Internet. Advertising may be supported by newspaper inserts and direct mail. Personal selling requires careful training of salespeople in how to greet customers, meet their needs, and handle their complaints. Sales promotions may include in-store demonstrations, displays, contests, and visiting celebrities. Public relations activities, such as press conferences and speeches, store openings, special events, newsletters, magazines, and public service activities, are always available to retailers. Most retailers have also set up Web sites, offering customers information and other features and often selling merchandise directly.

Real Marketing

At first glance, outdoor-products retailer Cabela's seems to break all the rules of retailing. First, it locates its stores in tiny, off-the-beaten-path locations—places like Sidney, Nebraska, Prairie du Chien, Wisconsin, Dundee, Michigan, Lehi, Utah, and Owatonna, Minnesota. Then, to make matters worse, it targets customers who hate to shop! The typical Cabela's customer is a reclusive male outdoorsman who yearns for the great outdoors, someone who detests jostling crowds and shopping.

So how do you explain Cabela's surging success? Over the past decade, Cabela's has evolved from a popular mail-order catalog business into one of the nation's hottest store retailers. Despite Cabela's often-remote locations, customers are flocking to its 15 superstores (soon to be 30) to buy hunting, fishing, and outdoor gear. A typical Cabela's store draws 4.4 million customers a year—an average of 40,000 customers on a Saturday and 50,000 to 100,000 on a holiday weekend. Half of Cabela's customers drive 100 miles or more to get there, and many travel up to 350 miles. Schools even send busloads of kids.



Cabela's: "This is more than a place to get fishhooks . . ."

In fact, Cabela's stores have become tourist destinations. Its store in Michigan is the state's largest tourist attraction, drawing more than 6 million people a year. The Minnesota store trails only the Mall of America in the number of annual visitors. And the Cabela's in Sidney, Nebraska, a town of only 6,000 people located 150 miles from the nearest city (Denver), attracts 1.2 millions visitors a year, making it Nebraska's second-largest tourist attraction behind The Omaha Zoo.

Just what is it that attracts these hordes of otherwise reluctant shoppers to Cabela's remote stores? Part of the answer lies in all the stuff the stores sell. Cabela's huge 230,000-square-foot superstores (one and one-half times larger than a typical Wal-Mart supercenter) house a vast assortment of quality merchandise at reasonable prices. Cabela's competes on price with discounters, but carries a selection that's six to ten times deeper—more than 200,000 kinds of items for hunting, fishing, boating, camping, and archery. "I'd have to go to two or three different stores to find all the brands they have at Cabela's," says Jason Gies, a 26-year-old mechanical engineer who drove 150 miles to purchase a vintage used Remington shotgun.

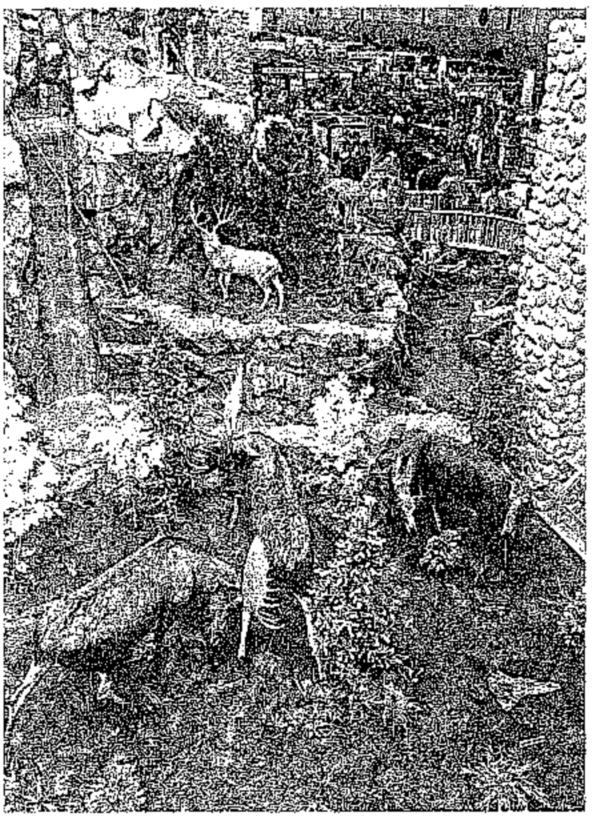
Cabela's also sells lines of branded clothing and gifts that appeal to customers' wives and children, making it a popular stop for the whole family. And to top things off, Cabela's offers first-class service. It staffs its departments with a generous supply of employees, all of whom must pass a 100-question test on the products they sell. For customers who stop by during hunting trips, Cabela's even offers use of outdoor kennels and corrals to house their hunting dogs or horses while they shop. Hunters with rifles are welcomed.

But deep product assortments and good service don't explain the huge crowds that show up at Cabela's. The retailer's real magic lies in the *experiences* it creates for those who visit. "This is more than a place to go get fishhooks," says a Cabela's spokesperson. "The Cabelas"—Nebraska brothers Dick and Jim—"wanted to create a sense of wonder." Mission accomplished! In each of its stores, Cabela's has created what amounts to a natural history theme park for outdoor enthusiasts.

Take the store near Fort Worth, Texas, for example, Cabela's 11th store and the largest so far. Dominating the center of the store is Conservation Mountain, a two-story mountain replica with two waterfalls and cascading streams. The mountain is divided into four ecosystems and five bioregions: a Texas prairie, an Alaskan habitat, an Arctic ice cap, an American woodland, and an Alpine mountaintop. Each bioregion is populated by lifelike, museum-quality taxidermy animals in action poses—everything from prairie dogs, deer,

Place Decision

Retailers often point to three critical factors in retailing success: *location, location,* and *location!* It's very important that retailers select locations that are accessible to the target market in areas that are consistent with the retailer's positioning. For example, Apple locates its stores in high-end malls and trendy shopping districts—such as the "Miracle Mile" on Chicago's Michigan Avenue or Fifth Avenue in Manhattan—not low-rent strip malls on the edge of town. Small retailers may have to settle for whatever locations they can find or afford. Large retailers, however, usually employ specialists who select locations using advanced methods.



". . . we want to create a sense of wonder."

elk, and caribou to brown bears, polar bears, musk oxen, and mountain goats.

Elsewhere in the store, Cabela's has created an African diorama, complete with African animals depicted in their natural habitats—an elephant, a rhinoceros, a Cape buffalo, and lions downing their prey. Other store attractions include a trophy deer museum and three walk-through aquariums, where visitors can view trophy-quality freshwater fish and learn to identify them. Getting hungry? Drop by the Mesquite Grill café for an elk, ostrich, or wild boar sandwich—no Big Macs here! The nearby General Store offers old-fashioned candy and snacks.

Cabela's spares no expense in developing this sportsman's paradise. A stuffed polar bear can cost up to $10,000. The Fort Worth store presents 800 such animals, right down to a Texas rattlesnake. Cabela's even created a new post—Taxidermy Purchasing Specialist—an executive who seeks out stuffed animals and mounts them in authentic scenes—two grizzly bears locked in battle, a leopard leaping for a monkey—even the droppings are real. "The muscle tone of the animal, the eyes, the posture—everything must be just right," says the executive. The taxidermy collection at Cabela's Fort Worth store is twice as large as the one at the Fort Worth Museum of Science and History.

So, if you scratch a little deeper, you find that far from breaking the rules, Cabela's is doing all the right things. It's creating total experiences that delight the senses as well as the wallets of carefully targeted customers. Put it all together and you've got a powerful magnet for outdoorsmen and their families. Just ask one of the millions of anything-but-reluctant Cabela's customers:

> "I'll do just about anything to avoid shopping," says John Brown, a small-business owner in Cheyenne, Wyoming. In 35 years of marriage, his wife says she's persuaded him to go shopping only twice. Yet one day last month he invited her to drive 100 miles with him for a day of shopping at Cabela's. "I'm like a kid in a candy store here," he says, dropping a new tackle box into his cart.
>
> The trick . . . is appealing to the family member who is usually most reluctant to shop: Dad. One recent morning, Lara Miller was trying to round up her husband and three kids, as their morning trip to Cabela's stretched into afternoon. Mrs. Miller—normally the only family member who likes to shop—now was the one most ready to leave. "We haven't had breakfast yet," she moaned. Her husband, Darren Miller, a farmer in Jerome, Idaho, said, "I love this place."

Sources: Extracts, quotes, and other information from Heather Landy, "Plenty in Store," *Knight Ridder Tribune Business News*, May 22, 2005, p. 1; Kevin Helliker, "Hunter Gatherer: Rare Retailer Scores by Targeting Men Who Hate to Shop," *Wall Street Journal*, December 17, 2002, p. A1; Landry, "Many Counting on New Cabela's to Be Quite a Draw," *Knight Ridder Tribune Business News*, May 22, 2005, p. 1; John Seward, "Outdoor Retailers Plan for Expansion," *Wall Street Journal*, June 8, 2005, p. 1, Bud Kennedy, "Bud Kennedy Column," *Fort Worth Star-Telegram*, May 26, 2005, p. 1; "The Art of Service," *Fast Company*, October 2005, pp. 47–58; Dan Benson, "Booming Times: Cabela's Pushes Up Interest, Price for Land in Area," *Milwaukee Journal Sentinel*, March 5, 2006; and www.cabelas.com, December 2006.

Most stores today cluster together to increase their customer pulling power and to give consumers the convenience of one-stop shopping. *Central business districts* were the main form of retail cluster until the 1950s. Every large city and town had a central business district with department stores, specialty stores, banks, and movie theaters. When people began to move to the suburbs, however, these central business districts, with their traffic, parking, and crime problems, began to lose business. Downtown merchants opened branches in suburban shopping centers, and the decline of the central business districts continued. In recent years, many cities have joined with merchants to try to revive downtown shopping areas by building malls and providing underground parking.

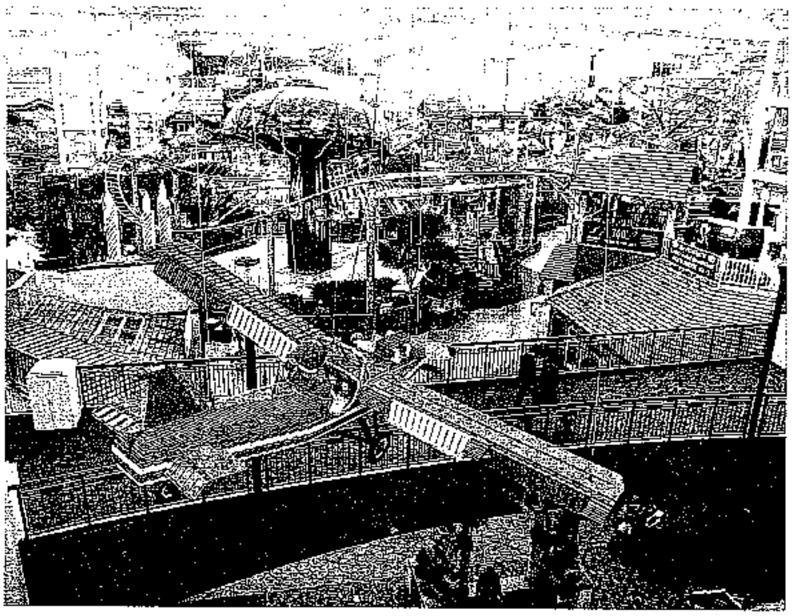
Shopping center
A group of retail businesses planned, developed, owned, and managed as a unit.

A **shopping center** is a group of retail businesses planned, developed, owned, and managed as a unit. A *regional shopping center*, or *regional shopping mall*, the largest and most dramatic shopping center, contains from 40 to over 200 stores. It is like a covered mini-downtown and attracts customers from a wide area. A *community shopping center* contains between 15 and 40 retail stores. It normally contains a branch of a department store or variety store, a supermarket, specialty stores, professional offices, and sometimes a bank. Most shopping centers are *neighborhood shopping centers* or *strip malls* that generally contain between 5 and 15 stores. They are close and convenient for consumers. They usually contain a supermarket, perhaps a discount store, and several service stores—dry cleaner, self-service laundry, drugstore, video-rental outlet, barber or beauty shop, hardware store, or other stores.

A recent addition to the shopping center scene is the so-called *power center*. These huge unenclosed shopping centers consist of a long strip of retail stores, including large, freestanding anchors such as Wal-Mart, Home Depot, Costco, Best Buy, Michaels, OfficeMax, and CompUSA. Each store has its own entrance with parking directly in front for shoppers who wish to visit only one store. Power centers have increased rapidly during the past few years to challenge traditional indoor malls.

Combined, the nation's nearly 48,500 shopping centers now account for about 75 percent of U.S. retail activity (not counting cars and gasoline). The average American makes 2.9 trips to the mall a month, shopping for an average of 80 minutes per trip and spending about $86. However, many experts suggest that America is now "over-malled." During the 1990s, mall shopping space grew at about twice the rate of population growth. As a result, as many as 20 percent of America's shopping malls are either dead or dying. There "is a glut of retail space," says one insider. "There's going to have to be a shakeout."[18]

Thus, despite the recent development of many new "megamalls," such as the spectacular Mall of America, the current trend is toward value-oriented outlet malls and power centers on the one hand, and smaller "lifestyle centers" on the other. These lifestyle centers—smaller malls with upscale stores, convenient locations, and expensive atmospheres—are usually located near affluent residential neighborhoods and cater to the retail needs of consumers in their areas. "Think of lifestyle centers as part Main Street and part Fifth Avenue," comments an industry observer. "The idea is to combine the hominess and community of an old-time village square with the cachet of fashionable urban stores; the smell and feel of a neighborhood park with the brute convenience of a strip center." The future of malls "will be all about creating places to be rather than just places to buy." [19]



Shopping centers: The spectacular Mall of America contains more than 520 specialty stores, 50 restaurants, a 7-acre indoor theme park, an Underwater World featuring hundreds of marine specimens and a dolphin show, and a two-story miniature golf course.

The Future of Retailing

Retailers operate in a harsh and fast-changing environment, which offers threats as well as opportunities. For example, the industry suffers from chronic overcapacity, resulting in fierce competition for customer dollars. Consumer demographics, lifestyles, and shopping patterns are changing rapidly, as are retailing technologies. To be successful, then, retailers will need to choose target segments carefully and position themselves strongly. They will need to take the following retailing developments into account as they plan and execute their competitive strategies.

New Retail Forms and Shortening Retail Life Cycles

New retail forms continue to emerge to meet new situations and consumer needs, but the life cycle of new retail forms is getting shorter. Department stores took about 100 years to reach the mature stage of the life cycle; more recent forms, such as warehouse stores, reached maturity in about 10 years. In such an environment, seemingly solid retail positions can crumble quickly. Of the top ten discount retailers in 1962 (the year that Wal-Mart and Kmart began), not one still exists today.

Consider the Price Club, the original warehouse store chain. When Sol Price pioneered his first warehouse store outside San Diego in 1976, he launched a retailing revolution. Selling everything from tires and office supplies to five-pound tubs of peanut butter at super low prices, his store chain was generating $2.6 billion a year in sales within 10 years. But Price refused to expand beyond its California base. And as the industry quickly matured, Price ran headlong into wholesale clubs run by such retail giants as Wal-Mart and Kmart. (In his autobiography, Sam Walton confesses: "I guess I've stolen—I actually prefer the word 'borrowed'—as many ideas from Sol Price as from anybody else in the business.") Only 17 years later, in a stunning reversal of fortune, a faltering Price sold out to competitor Costco. Price's rapid rise and fall shows that even the most successful retailers can't sit back with a winning formula. To remain successful, they must keep adapting.[20]

Wheel-of-retailing concept
A concept of retailing that states that new types of retailers usually begin as low-margin, low-price, low-status operations but later evolve into higher-priced, higher-service operations, eventually becoming like the conventional retailers they replaced.

Many retailing innovations are partially explained by the **wheel-of-retailing concept.**[21] According to this concept, many new types of retailing forms begin as low-margin, low-price, low-status operations. They challenge established retailers that have become "fat" by letting their costs and margins increase. The new retailers' success leads them to upgrade their facilities and offer more services. In turn, their costs increase, forcing them to increase their prices. Eventually, the new retailers become like the conventional retailers they replaced. The cycle begins again when still newer types of retailers evolve with lower costs and prices. The wheel-of-retailing concept seems to explain the initial success and later troubles of department stores, supermarkets, and discount stores and the recent success of off-price retailers.

Growth of Nonstore Retailing

Most of us still make most of our purchases the old-fashioned way: We go to the store, find what we want, wait patiently in line to plunk down our cash or credit card, and bring home the goods. However, consumers now have an array of alternatives, including mail-order, television, phone, and online shopping. Americans are increasingly avoiding the hassles and crowds at malls by doing more of their shopping by phone or computer. Although such retailing advances may threaten some traditional retailers, they offer exciting opportunities for others. Most store retailers have now developed direct-retailing channels. In fact, more online retailing is conducted by "click-and-brick" retailers than by "click-only" retailers. In a recent ranking of the top 50 online retail sites, 35 were multichannel retailers.[22]

Online retailing is the newest form of nonstore retailing. Only a few years ago, prospects for online retailing were soaring. As more and more consumers flocked to the Web, some experts even saw a day when consumers would bypass stodgy "old economy" store retailers and do almost all of their shopping via the Internet. However, the dot-com meltdown of 2000 dashed these overblown expectations. Many once-brash Web sellers crashed and burned and expectations reversed almost overnight. The experts began to predict that e-tailing was destined to be little more than a tag-on to in-store retailing.

However, today's online retailing is alive, well, and growing. With easier-to-use Web sites, improved online service, and the increasing sophistication of search technologies, online business is booming. In fact, online buying is growing at a much brisker pace than retail buying as a whole. Last year's U.S. online retail sales reached $113.6 billion, a 28 percent leap over the previous year, representing 4.7 percent of all retail sales.[23]

All types of retailers now use the Web as an important marketing tool. The online sales of giant brick-and-mortar retailers, such as Sears, Wal-Mart, Staples, and Gap, are increasing rapidly. Several large click-only retailers—Amazon.com, online auction site eBay, online travel companies such as Travelocity and Expedia, and others—are now making it big on the Web. At the other extreme, hordes of niche marketers are using the Web to reach new markets and expand their sales. Today's more sophisticated search engines (Google, Yahoo!) and comparison shopping sites (Shopping.com, Buy.com, Shopzilla, and others) put almost any e-tailer within a mouse click or two's reach of millions of customers.

Online retailing: Today's online retailing is alive, well, and growing, especially for click-and-brick retailers like Staples. Its Web site, staples.com, now accounts for almost one-quarter of sales. "That was easy!"

Still, much of the anticipated growth in online sales will go to multichannel retailers—the click-and-brick marketers who can successfully merge the virtual and physical worlds. Consider office-supply retailer Staples. Based on two years of research, Staples recently redesigned its Web site to extend its "Staples—That was easy" marketing promise to online shoppers. The retailer's online sales are now growing at an even faster clip than its store sales. Sales through Staples.com jumped 27 percent last year, now accounting for almost one-quarter of Staples's revenues. But Staples online operations aren't robbing from store sales. Instead, the in-store and online channels compliment one another. For example, customers can buy conveniently online and then return unwanted or defective merchandise to their local Staples store. And in-store Staples.com kiosks ensure that customers never leave the store without finding what they need. As a result, for example, the average yearly spending of small-business customers jumps more than fourfold when they combine shopping online with shopping in the store.[24]

Retail Convergence

Today's retailers are increasingly selling the same products at the same prices to the same consumers in competition with a wider variety of other retailers. For example, you can buy books at outlets ranging from independent local bookstores to warehouse clubs such as Costco, superstores such as Barnes & Noble or Borders, or Web sites such as Amazon.com. When it comes to brand-name appliances, department stores, discount stores, home improvement stores, off-price retailers, electronics superstores, and a slew of Web sites all compete for the same customers. So if you can't find the microwave oven you want at Sears, just step across the street and find one for a better price at Lowe's or Home Depot—or just order one online from Amazon.com.

This merging of consumers, products, prices, and retailers is called *retail convergence*. "Where you go for what you want—that has created the biggest challenge facing retailers," says one retailing expert. "Customers of all income levels are shopping at the same stores, often for the same goods. Old distinctions such as discount store, specialty store, and department store are losing significance: The successful store must match a host of rivals on selection, service, and price."[25]

Such convergence means greater competition for retailers and greater difficulty in differentiating offerings. The competition between chain superstores and smaller, independently owned stores has become particularly heated. Because of their bulk-buying power and high sales volume, chains can buy at lower costs and thrive on smaller margins. The arrival of a superstore can quickly force nearby independents out of business. For example, the decision by electronics superstore Best Buy to sell CDs as loss leaders at rock-bottom prices pushed a number of specialty record-store chains into bankruptcy. And with its everyday low prices, Wal-Mart has been accused of destroying independents in countless small towns around the country who sell the same merchandise.

Yet the news is not all bad for smaller companies. Many small, independent retailers are thriving. They are finding that sheer size and marketing muscle are often no match for the personal touch small stores can provide or the specialty merchandise niches that small stores fill for a devoted customer base.

The Rise of Megaretailers

The rise of huge mass merchandisers and specialty superstores, the formation of vertical marketing systems, and a rash of retail mergers and acquisitions have created a core of superpower megaretailers. Through their superior information systems and buying power, these giant retailers can offer better merchandise selections, good service, and strong price savings to consumers. As a result, they grow even larger by squeezing out their smaller, weaker competitors.

The megaretailers are also shifting the balance of power between retailers and producers. A relative handful of retailers now control access to enormous numbers of consumers, giving them the upper hand in their dealings with manufacturers. For example, in the United States, Wal-Mart's revenues are more than five times those of Procter & Gamble, and Wal-Mart generates almost 20 percent of P&G's revenues. Wal-Mart can, and often does, use this power to wring concessions from P&G and other suppliers.[26]

Growing Importance of Retail Technology

Retail technologies are becoming critically important as competitive tools. Progressive retailers are using advanced information technology and software systems to produce better forecasts, control inventory costs, order electronically from suppliers, send information between stores, and even sell to customers within stores. They are adopting checkout scanning systems, online transaction processing, electronic data interchange, in-store television, and improved merchandise-handling systems.

Perhaps the most startling advances in retailing technology concern the ways in which today's retailers are connecting with customers. Many retailers now routinely use technologies such as touch-screen kiosks, customer-loyalty cards, electronic shelf labels and signs, handheld shopping assistants, smart cards, self-scanning systems, and virtual-reality displays. For example, in its new pilot store—Bloom—southeastern grocery chain Food Lion is using technology to make shopping easier for its customers:

> Ever stood in the wine aisle at the grocery store and felt intimidated? You think that bottle of Shiraz looks pretty good but you're not sure what it goes with. It's the sort of problem the creators of Food Lion's new concept store —Bloom—thought about, and one they will use technology to solve. The store relies on technology to enhance the shopping experience and to help customers find products, get information, and check out with greater ease. A computerized kiosk in the wine section lets you scan a bottle and get serving suggestions. The kiosk, and a second one in the meat section, lets you print recipes off the screen. Eight stations with touch screens and scanners around the store let you check an item's price or locate it on the map. To make it easier to keep track of purchases and check out, you can pick up a personal handheld scanner as you walk in the door, then scan and bag items as you shop. Checkout then is just a simple matter of paying as you leave. The personal scanners also give you a running total of the items you've selected as you shop, helping you stay within your budget and avoid surprises at the checkout. And if you drop off a prescription, the pharmacy can send a message to your scanner when your order is ready.[27]

Retail technology: In its new pilot store—Bloom—Southeastern grocery chain Food Lion is using technology to make shopping easier for its customers.

Global Expansion of Major Retailers

Retailers with unique formats and strong brand positioning are increasingly moving into other countries. Many are expanding internationally to escape mature and saturated home markets. Over the years, some giant U.S. retailers, such as McDonald's, have become globally prominent as a result of their marketing prowess. Others, such as Wal-Mart, are rapidly establishing a global presence. Wal-Mart, which now operates more than 2,700 stores in 14 countries abroad, sees exciting global potential. Its international division alone last year racked up sales of more than $67 billion, an increase of 11.4 percent over the previous year and 27 percent more than rival Target's *total* sales. Profits from international operations increased more than 26 percent last year.[28]

However, most U.S retailers are still significantly behind Europe and Asia when it comes to global expansion. Ten of the world's top 20 retailers are U.S. companies; only two of these retailers have set up stores outside of North America (Wal-Mart and Costco). Of the 10 non-U.S. retailers in the world's top 20, nine have stores in at least 10 countries. Among foreign retailers that have gone global are France's Carrefour, Germany's Metro and Aldi chains, the Netherlands' Royal Ahold, Britain's Tesco, Japan's Yaohan supermarkets, and Sweden's IKEA home furnishings stores.[29]

French discount retailer Carrefour, the world's second-largest retailer after Wal-Mart, has embarked on an aggressive mission to extend its role as a leading international retailer:

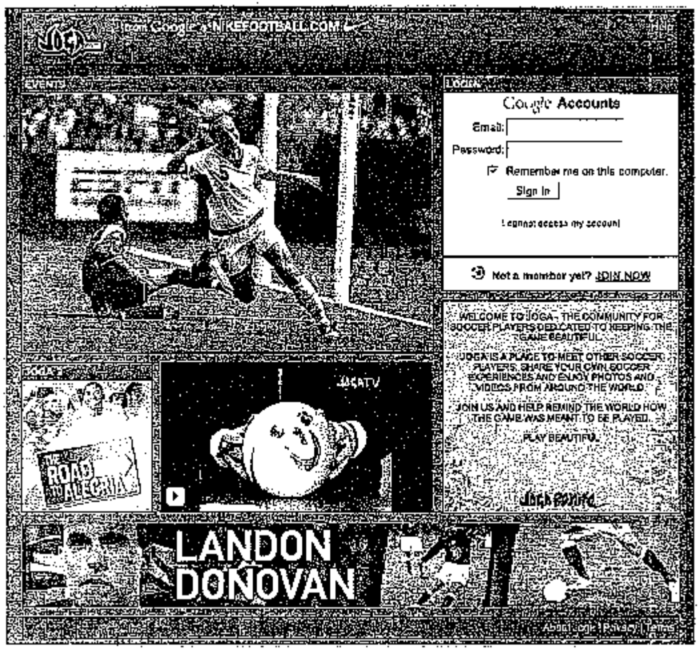
> The Carrefour Group has an interest in more than 12,000 stores in 29 countries in Europe, Asia, and the Americas, including 926 hypermarkets. It leads Europe in supermarkets and the world in hypermarkets. Carrefour is outpacing Wal-Mart in several emerging markets, including South America, China, and the Pacific Rim. It's the leading retailer in Brazil and Argentina, where it operates close to 1,000 stores, compared to Wal-Mart's 300 units in those two countries. Carrefour is the largest foreign retailer in China, where it operates more than 300 stores versus Wal-Mart's 60. In short, Carrefour is forging ahead of Wal-Mart in most markets outside North America. The only question: Can the French retailer hold its lead? Although no one retailer can safely claim to be in the same league with Wal-Mart as an overall retail presence, Carrefour stands a better chance than most to hold its own in global retailing.[30]

Retail Stores as "Communities" or "Hangouts"

With the rise in the number of people living alone, working at home, or living in isolated and sprawling suburbs, there has been a resurgence of establishments that, regardless of the product or service they offer, also provide a place for people to get together. These places include coffee shops and cafes, shopping malls, bookstores, children's play spaces, superstores, and urban greenmarkets. For example, today's bookstores have become part bookstore, part library, part living room, and part coffee house. On an early evening at your local Barnes & Noble, you'll likely find back-pack-toting high school students doing homework with friends in the coffee bar. Nearby, retirees sit in cushy chairs thumbing through travel or gardening books while parents read aloud to their children. Barnes & Noble sells more than just books, it sells comfort, relaxation, and community.

And retailers don't create communities only in their brick-and-mortar stores. Many also build virtual communities on the Internet. For example, Nike creates community in its giant, interactive Niketown retail stores, but it also creates online gathering places:

> In just over a decade, Nike's global soccer presence has grown dramatically—from roughly $40 million of sales in 1994 to almost $1.5 billion today. So, when Nike discovered that rival Adidas had gotten the exclusive deal to broadcast ads in the United States during the 2006 World Cup, it had to be innovative. In partnership with Google, Nike created Joga.com, a social networking site for soccer fans. Launched quietly in February of 2006, the site became an instant hit—a bustling online soccer community. More than 1 million members from 140 countries signed up by mid-July. On Joga.com, fans can blog, create communities around favorite teams or players, organize pickup games, download videos, and rant about the encroaching commercialism of the game. Some of the most downloaded videos are clips containing Nike products. According to one marketing analyst, "By enrolling consumers in shaping the [content], Nike is . . . nurturing deeper bonds of loyalty and advocacy." Nike's CEO agrees: "When someone joins a Nike community or invites Nike into their community, a strong relationship is created."[31]



Nike creates community in its giant, interactive Niketown retail stores, but it also creates community in its online gathering place, Joga.com, a social networking site that allows soccer fans to blog, create communities around favorite teams or players, organize pickup games, download videos, and rant about the encroaching commercialism of the game.

Wholesaling

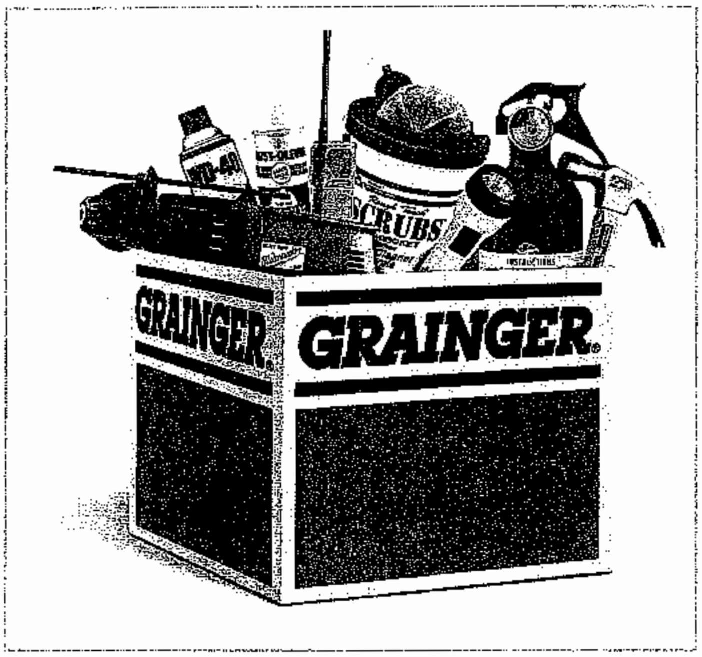
Wholesaling
All activities involved in selling goods and services to those buying for resale or business use.

Wholesaler
A firm engaged *primarily* in wholesaling activities.

Wholesaling includes all activities involved in selling goods and services to those buying for resale or business use. We call **wholesalers** those firms engaged *primarily* in wholesaling activities.

Wholesalers buy mostly from producers and sell mostly to retailers, industrial consumers, and other wholesalers. As a result, many of the nation's largest and most important wholesalers are largely unknown to final consumers. For example, you may never have heard of Grainger, even though it's very well known and much valued by its more than 1.7 million business and institutional customers across North America.

> Grainger may be the biggest market leader you've never heard of. It's a $5.5 billion business that offers more than 800,000 maintenance, repair, and operating (MRO) products to more than 1.7 million customers. Through its branch network, service centers, sales reps, catalog, and Web site, Grainger links customers with the supplies they need to keep their facilities running smoothly—everything from light bulbs, cleaners, and display cases to nuts and bolts, motors, valves, power tools, and test equipment. Grainger's nearly 600 North American branches, 20 distribution centers, more than 16,700 employees, and innovative Web site handle more than 100,000 transactions a day. Its customers include organizations ranging from factories, garages, and grocers to schools and military bases. Most American businesses are located within 20 minutes of a Grainger branch. Customers include notables such as Abbott Laboratories, General Motors, Campbell Soup, American Airlines, DaimlerChrysler, and the U.S. Postal Service.
>
> Grainger operates on a simple value proposition: to make it easier and less costly for customers to find and buy MRO supplies. It starts by acting as a one-stop shop for products to maintain facilities. On a broader level, it builds lasting relationships with customers by helping them find *solutions* to their overall MRO problems. Acting as consultants, Grainger sales reps help buyers with everything from improving their supply chain management to reducing inventories and streamlining warehousing operations. So, how come you've never heard of Grainger? Maybe it's because the company operates in the not-so-glamorous world of MRO supplies, which are important to every business but not so important to consumers. More likely, it's because Grainger is a wholesaler. And like most wholesalers, it operates behind the scenes, selling only to other businesses.[32]



Wholesaling: Many of the nation's largest and most important wholesalers—like Grainger—are largely unknown to final consumers. But they are very well known and much valued by the business customers they serve.

Why are wholesalers important to sellers? For example, why would a producer use wholesalers rather than selling directly to retailers or consumers? Simply put, wholesalers add value by performing one or more of the following channel functions:

- *Selling and promoting:* Wholesalers' sales forces help manufacturers reach many small customers at a low cost. The wholesaler has more contacts and is often more trusted by the buyer than the distant manufacturer.
- *Buying and assortment building:* Wholesalers can select items and build assortments needed by their customers, thereby saving the consumers much work.
- *Bulk-breaking:* Wholesalers save their customers money by buying in carload lots and breaking bulk (breaking large lots into small quantities).
- *Warehousing:* Wholesalers hold inventories, thereby reducing the inventory costs and risks of suppliers and customers.
- *Transportation:* Wholesalers can provide quicker delivery to buyers because they are closer than the producers.
- *Financing:* Wholesalers finance their customers by giving credit, and they finance their suppliers by ordering early and paying bills on time.
- *Risk bearing:* Wholesalers absorb risk by taking title and bearing the cost of theft, damage, spoilage, and obsolescence.
- *Market information:* Wholesalers give information to suppliers and customers about competitors, new products, and price developments.
- *Management services and advice:* Wholesalers often help retailers train their salesclerks, improve store layouts and displays, and set up accounting and inventory control systems.

Types of Wholesalers

Merchant wholesaler
Independently owned business that takes title to the merchandise it handles.

Wholesalers fall into three major groups (see Table 13.3): *merchant wholesalers, agents and brokers,* and *manufacturers' sales branches and offices.* **Merchant wholesalers** are the largest single group of wholesalers, accounting for roughly 50 percent of all wholesaling. Merchant wholesalers include two broad types: full-service wholesalers and limited-service wholesalers. *Full-service wholesalers* provide a full set of services, whereas the various *limited-service wholesalers* offer fewer services to their suppliers and customers. The several different

TABLE 13.3 Major Types of Wholesalers

Type	Description
Merchant wholesalers	Independently owned businesses that take title to the merchandise they handle. In different trades they are called *jobbers, distributors,* or *mill supply houses.* They include *full-service wholesalers* and *limited-service wholesalers.*
Full-service wholesalers	Provide a full line of services: carrying stock, maintaining a sales force, offering credit, making deliveries, and providing management assistance. There are two types:
Wholesale merchants	Sell primarily to retailers and provide a full range of services. *General merchandise wholesalers* carry several merchandise lines, whereas *general line wholesalers* carry one or two lines in great depth. *Specialty wholesalers* specialize in carrying only part of a line. Examples: health food wholesalers, seafood wholesalers.
Industrial distributors	Sell to manufacturers rather than to retailers. Provide several services, such as carrying stock, offering credit, and providing delivery. May carry a broad range of merchandise, a general line, or a specialty line.
Limited-service wholesalers	Offer fewer services than full-service wholesalers. Limited-service wholesalers are of several types:
Cash-and-carry wholesalers	Carry a limited line of fast-moving goods and sell to small retailers for cash. Normally do not deliver. Example: A small fish store retailer may drive to a cash-and-carry fish wholesaler, buy fish for cash, and bring the merchandise back to the store.
Truck wholesalers (or truck jobbers)	Perform primarily a selling and delivery function. Carry limited line of semiperishable merchandise (such as milk, bread, snack foods), which they sell for cash as they make their rounds to supermarkets, small groceries, hospitals, restaurants, factory cafeterias, and hotels.
Drop shippers	Do not carry inventory or handle the product. On receiving an order, they select a manufacturer, who ships the merchandise directly to the customer. The drop shipper assumes title and risk from the time the order is accepted to its delivery to the customer. They operate in bulk industries, such as coal, lumber, and heavy equipment.
Rack jobbers	Serve grocery and drug retailers, mostly in nonfood items. They send delivery trucks to stores, where the delivery people set up toys, paperbacks, hardware items, health and beauty aids, or other items. They price the goods, keep them fresh, set up point-of-purchase displays, and keep inventory records. Rack jobbers retain title to the goods and bill the retailers only for the goods sold to consumers.
Producers' cooperatives	Are owned by farmer members and assemble farm produce to sell in local markets. The co-op's profits are distributed to members at the end of the year. They often attempt to improve product quality and promote a co-op brand name, such as Sun Maid raisins, Sunkist oranges, or Diamond walnuts.
Mail-order wholesalers	Send catalogs to retail, industrial, and institutional customers featuring jewelry, cosmetics, specialty foods, and other small items. Maintain no outside sales force. Main customers are businesses in small outlying areas. Orders are filled and sent by mail, truck, or other transportation.
Brokers and agents	Do not take title to goods. Main function is to facilitate buying and selling, for which they earn a commission on the selling price. Generally specialize by product line or customer type.
Brokers	Chief function is bringing buyers and sellers together and assisting in negotiation. They are paid by the party who hired them and do not carry inventory, get involved in financing, or assume risk. Examples: food brokers, real estate brokers, insurance brokers, and security brokers.
Agents	Represent either buyers or sellers on a more permanent basis than brokers do. There are several types:
Manufacturers' agents	Represent two or more manufacturers of complementary lines. A formal written agreement with each manufacturer covers pricing, territories, order handling, delivery service and warranties, and commission rates. Often used in such lines as apparel, furniture, and electrical goods. Most manufacturers' agents are small businesses, with only a few skilled salespeople as employees. They are hired by small manufacturers who cannot afford their own field sales forces and by large manufacturers who use agents to open new territories or to cover territories that cannot support full-time salespeople.

(continues)

TABLE 13.3 Major Types of Wholesalers—*continued*

Type	*Description*
Selling agents	Have contractual authority to sell a manufacturer's entire output. The manufacturer either is not interested in the selling function or feels unqualified. The selling agent serves as a sales department and has significant influence over prices, terms, and conditions of sale. Found in product areas such as textiles, industrial machinery and equipment, coal and coke, chemicals, and metals.
Purchasing agents	Generally have a long-term relationship with buyers and make purchases for them, often receiving, inspecting, warehousing, and shipping the merchandise to the buyers. They provide helpful market information to clients and help them obtain the best goods and prices available.
Commission merchants	Take physical possession of products and negotiate sales. Normally, they are not employed on a long-term basis. Used most often in agricultural marketing by farmers who do not want to sell their own output and do not belong to producers' cooperatives. The commission merchant takes a truckload of commodities to a central market, sells it for the best price, deducts a commission and expenses, and remits the balance to the producers.
Manufacturers' and retailers' branches and offices	Wholesaling operations conducted by sellers or buyers themselves rather than through independent wholesalers. Separate branches and offices can be dedicated to either sales or purchasing.
Sales branches and offices	Set up by manufacturers to improve inventory control, selling, and promotion. *Sales branches* carry inventory and are found in industries such as lumber and automotive equipment and parts. *Sales offices* do not carry inventory and are most prominent in dry-goods and notions industries.
Purchasing officers	Perform a role similar to that of brokers or agents but are part of the buyer's organization. Many retailers set up purchasing offices in major market centers such as New York and Chicago.

types of limited-service wholesalers perform varied specialized functions in the distribution channel.

Brokers and *agents* differ from merchant wholesalers in two ways: They do not take title to goods, and they perform only a few functions. Like merchant wholesalers, they generally specialize by product line or customer type. A **broker** brings buyers and sellers together and assists in negotiation. **Agents** represent buyers or sellers on a more permanent basis. *Manufacturers' agents* (also called manufacturers' representatives) are the most common type of agent wholesaler. The third major type of wholesaling is that done in **manufacturers' sales branches and offices** by sellers or buyers themselves rather than through independent wholesalers.

Broker
A wholesaler who does not take title to goods and whose function is to bring buyers and sellers together and assist in negotiation.

Agent
A wholesaler who represents buyers or sellers on a relatively permanent basis, performs only a few functions, and does not take title to goods.

Manufacturers' sales branches and offices
Wholesaling by sellers or buyers themselves rather than through independent wholesalers.

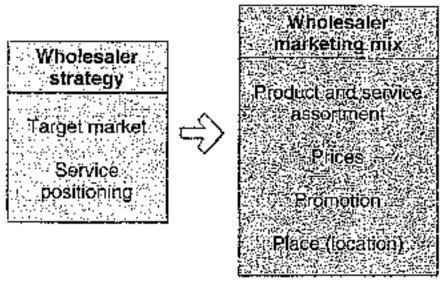
Wholesaler Marketing Decisions

Wholesalers now face growing competitive pressures, more demanding customers, new technologies, and more direct-buying programs on the part of large industrial, institutional, and retail buyers. As a result, they have taken a fresh look at their marketing strategies. As with retailers, their marketing decisions include choices of target markets, positioning, and the marketing mix—product assortments and services, price, promotion, and place (see Figure 13.2).

Target Market and Positioning Decision

Like retailers, wholesalers must define their target markets and position themselves effectively—they cannot serve everyone. They can choose a target group by size of customer (only large retailers), type of customer (convenience stores only), need for service (customers who need credit), or other factors. Within the target group, they can identify the more profitable customers, design stronger offers, and build better relationships with them. They can propose automatic reordering systems, set up management-training and advising systems, or even sponsor a voluntary chain. They can discourage less profitable customers by requiring larger orders or adding service charges to smaller ones.

FIGURE 13.2
Wholesaler marketing decisions



Marketing Mix Decisions

Like retailers, wholesalers must decide on product assortment and services, prices, promotion, and place. The wholesaler's "product" is the assortment of *products and services* that it offers. Wholesalers are under great pressure to carry a full line and to stock enough for immediate delivery. But this practice can damage profits. Wholesalers today are cutting down on the number of lines they carry, choosing to carry only the more profitable ones. Wholesalers are also rethinking which services count most in building strong customer relationships and which should be dropped or charged for. The key is to find the mix of services most valued by their target customers.

Price is also an important wholesaler decision. Wholesalers usually mark up the cost of goods by a standard percentage—say, 20 percent. Expenses may run 17 percent of the gross margin, leaving a profit margin of 3 percent. In grocery wholesaling, the average profit margin is often less than 2 percent. Wholesalers are trying new pricing approaches. They may cut their margin on some lines in order to win important new customers. They may ask suppliers for special price breaks when they can turn them into an increase in the supplier's sales.

Although *promotion* can be critical to wholesaler success, most wholesalers are not promotion minded. Their use of trade advertising, sales promotion, personal selling, and public relations is largely scattered and unplanned. Many are behind the times in personal selling—they still see selling as a single salesperson talking to a single customer instead of as a team effort to sell, build, and service major accounts. Wholesalers also need to adopt some of the nonpersonal promotion techniques used by retailers. They need to develop an overall promotion strategy and to make greater use of supplier promotion materials and programs.

Finally, *place* is important—wholesalers must choose their locations, facilities, and Web locations carefully. Wholesalers typically locate in low-rent, low-tax areas and tend to invest little money in their buildings, equipment, and systems. As a result, their materials-handling and order-processing systems are often outdated. In recent years, however, large and progressive wholesalers are reacting to rising costs by investing in automated warehouses and online ordering systems. Orders are fed from the retailer's system directly into the wholesaler's computer, and the items are picked up by mechanical devices and automatically taken to a shipping platform where they are assembled. Most large wholesalers are using technology to carry out accounting, billing, inventory control, and forecasting. Modern wholesalers are adapting their services to the needs of target customers and finding cost-reducing methods of doing business.

Trends in Wholesaling

Today's wholesalers face considerable challenges. The industry remains vulnerable to one of the most enduring trends of the last decade—fierce resistance to price increases and the winnowing out of suppliers who are not adding value based on cost and quality. Progressive wholesalers constantly watch for better ways to meet the changing needs of their suppliers and target customers. They recognize that, in the long run, their only reason for existence comes from adding value by increasing the efficiency and effectiveness of the entire marketing channel. For example, Grainger succeeds by making life easier and more efficient for the commercial and institutional buyers and sellers it serves:

> Beyond making it easier for customers to find the products they need, Grainger also helps them streamline their acquisition processes. For most companies, acquiring MRO supplies is a very costly process. In fact, 40 percent of the cost of MRO supplies stems from the purchase process, including finding a supplier, negotiating the best deal, placing the order, receiving the order, and paying the invoice. Grainger constantly seeks ways to reduce the costs associated with MRO supplies acquisition, both internally and

externally. One company found that working with Grainger cut MRO requisition time by more than 60 percent; lead times went from days to hours. Its supply chain dropped from 12,000 suppliers to 560—significantly reducing expenses. Similarly, a large timber and paper-products company has come to appreciate Grainger's selection and streamlined ordering process. It orders two-thirds of its supplies from Grainger's Web site at an annual acquisition cost of only $300,000. By comparison, for the remainder of its needs, this company deals with more than 1,300 small distributors at an acquisition cost of $2.4 million each year—eight times the cost of dealing with Grainger for half of the volume. The company is now looking for ways to buy all of its MRO supplies from Grainger. As one Grainger branch manager puts it, "If we don't save [customers] time and money every time they come [to us], they won't come back."[33]

McKesson, the nation's leading wholesaler of pharmaceuticals, health and beauty care, home health care, and medical supply and equipment products, provides another example of progressive, value-adding wholesaling. To survive, McKesson has to remain more cost effective than manufacturers' sales branches. Thus, the company has built efficient automated warehouses, established direct computer links with drug manufacturers, and set up extensive online supply-management and accounts-receivable systems for customers. It offers retail pharmacists a wide range of online resources, including supply-management assistance, catalog searches, real-time order tracking, and an account-management system. It has also created solutions such as automated pharmaceutical-dispensing machines that assist pharmacists by reducing costs and improving accuracy.

Retailers can even use the McKesson system to maintain medical profiles on their customers. McKesson's medical-surgical supply and equipment customers receive a rich assortment of online solutions and supply-management tools, including an online order-management system and real-time information on products and pricing, inventory availability, and order status. According to McKesson, it adds value in the channel by providing "supply, information, and health-care-management products and services designed to reduce costs and improve quality across health care."[34]

The distinction between large retailers and large wholesalers continues to blur. Many retailers now operate formats such as wholesale clubs and hypermarkets that perform many wholesale functions. In return, many large wholesalers are setting up their own retailing operations. For example, until recently, SuperValu was classified as a food wholesaler, with a majority of its business derived from supplying grocery products to independent grocery retailers. However, over the past decade, SuperValu has started or acquired several retail food chains of its own—including Albertsons, Jewel-Osco, Save-A-Lot, Cub Foods, and others—to become the nation's third-largest food retailer. Thus, even though it remains the country's largest food wholesaler, because 80 percent of its $44 billion in sales come from retailing, SuperValu is now classified as a retailer.[35]

Wholesalers will continue to increase the services they provide to retailers—retail pricing, cooperative advertising, marketing and management information reports, accounting services, online transactions, and others. Rising costs on the one hand, and the demand for increased services on the other, will put the squeeze on wholesaler profits. Wholesalers who do not find efficient ways to deliver value to their customers will soon drop by the wayside. However, the increased use of computerized, automated, and Web-based systems will help wholesalers to contain the costs of ordering, shipping, and inventory holding, boosting their productivity.

Finally, facing slow growth in their domestic markets and such developments as the North American Free Trade Agreement, many large wholesalers are now going global. For example, in 1991, McKesson bought out its Canadian partner, Provigo. The company now receives about 3 percent of its total revenues from Canada. Its Information Solutions group operates widely throughout North America, the United Kingdom, and other European countries.

Reviewing the Concepts

In this chapter, we looked at the nature and importance of retailing, major types of retailers, the decisions retailers make, and the future of retailing. We then examined these same topics for wholesalers.

1. **Explain the roles of retailers and wholesalers in the distribution channel.** Retailing and wholesaling consist of many organizations bringing goods and services from the point of production to the point of use. *Retailing* includes all activities involved in selling goods or services directly to final consumers for their personal, nonbusiness use. *Wholesaling* includes all the activities involved in selling goods or services to those who are buying for the purpose of resale or for business use. Wholesalers perform many functions, including selling and promoting, buying and assortment building, bulk breaking, warehousing, transporting, financing, risk bearing, supplying market information, and providing management services and advice.

2. **Describe the major types of retailers and give examples of each.** Retail stores come in all shapes and sizes, and new retail types keep emerging. Store retailers can be classified by *the amount of service* they provide (self-service, limited service, or full service), *product line sold* (specialty stores, department stores, supermarkets, convenience stores, superstores, and service businesses), and *relative prices* (discount stores and off-price retailers). Today, many retailers are banding together in corporate and contractual *retail organizations* (corporate chains, voluntary chains and retailer cooperatives, franchise organizations, and merchandising conglomerates).

3. **Describe the major types of wholesalers and give examples of each.** Wholesalers fall into three groups. First, *merchant wholesalers* take possession of the goods. They include *full-service wholesalers* (wholesale merchants, industrial distributors) and *limited-service wholesalers* (cash-and-carry wholesalers, truck wholesalers, drop shippers, rack jobbers, producers' cooperatives, and mail-order wholesalers). Second, *brokers* and *agents* do not take possession of the goods but are paid a commission for aiding buying and selling. Finally, *manufacturers' sales branches and offices* are wholesaling operations conducted by nonwholesalers to bypass the wholesalers.

4. **Explain the marketing decisions facing retailers and wholesalers.** Each retailer must make decisions about its target markets and positioning, product assortment and services, price, promotion, and place. Retailers need to choose target markets carefully and position themselves strongly. Today, wholesaling is holding its own in the economy. Progressive wholesalers are adapting their services to the needs of target customers and are seeking cost-reducing methods of doing business. Faced with slow growth in their domestic markets and developments such as the North American Free Trade Agreement, many large wholesalers are also now going global.

Reviewing the Key Terms

Agent 388
Broker 388
Category killer 369
Chain stores 372
Convenience store 368
Department store 368
Discount store 370
Factory outlet 371
Franchise 373
Independent off-price retailer 371
Manufacturers' sales branches and offices 388
Merchant wholesaler 386
Off-price retailer 370
Retailer 367
Retailing 367
Shopping center 380
Specialty store 368
Supermarket 368
Superstore 369
Warehouse club 372
Wheel-of-retailing concept 381
Wholesaler 385
Wholesaling 385

Discussing the Concepts

1. Why have warehouse clubs grown in popularity over the past several years?
2. Describe the similarities and differences between corporate chain stores and franchise organizations.
3. Explain why it is important for retailers to define their target markets and to decide how they will position themselves in these markets. Give an example of a national specialty retailer that has done this well.
4. What is the wheel-of-retailing concept? Does it apply to online retailing?
5. What is retail convergence? How has it helped or harmed small retailers?
6. What is the primary challenge facing a wholesaler who wishes to remain a viable part of the marketing channel? Explain.

Applying the Concepts

1. Choose three retailers that you buy from often. Classify these retailers in terms of the characteristics presented in the chapter. Next, use Table 13.1 to categorize each retailer.
2. Jordan's Furniture differentiates itself through its store atmosphere. Visit it on the Web at www.jordans.com and take a virtual tour of its Natick store. Does Jordan's Furniture do a good job of differentiating itself?
3. Suppose that you are a manufacturer's agent for three lines of complementary women's apparel. Discuss what types of marketing mix decisions you will be making.

Focus on Technology

Imagine having a friend who helps you with your grocery shopping by reminding you about how much you have spent, what you usually purchase, and what's on sale this week that you have purchased in the past. Stop & Shop Supermarket Company, the largest food retailer in New England, will soon introduce the Shopping Buddy. According to the company, "Shopping Buddy can help you organize your shopping trip and save money! The Shopping Buddy is a small tablet that you activate with your Stop & Shop card. Once activated, the Shopping Buddy displays your personal savings coupons and shopping history by aisle, based on your location. It's easy to see the things that you normally buy that are on sale in each aisle. You can also use Buddy to keep a running total of today's purchases, order deli without waiting in line, and scan and bag your items as you shop for quick checkout." Stop & Shop will soon be testing this new technology in 20 of its 360 stores.

1. What advantages does Stop & Shop gain by offering this technology?
2. What do you think of the Shopping Buddy concept? Would you use this technology?
3. Visit Stop & Shop at www.stopandshop.com. What other services does this retailer offer that differentiate its store from competitors' stores?

Focus on Ethics

Purchase a television, computer, or other electronic device and you are bound to be asked whether you would like to purchase a service contract. Most large electronics retailers carefully train their salespeople and cashiers to ask this important question. In fact, some retailers urge their salespeople to exert strong sales pressure to sell these contracts. It's no wonder, because service contracts provide extremely high profits for the retailers, several times the profit margins realized from the equipment you are purchasing. But do you know when to say yes and when to pass on a contract? Most consumers are confused and will buy the contract because the price seems low in comparison to the price of that new plasma television. Experts, such as those at Consumer Reports, generally recommend that buyers pass on these contracts. With increased product reliability and decreasing prices that make replacement more reasonable, such contracts are rarely worth the price. If most consumers do not need them, should retailers continue to offer and promote them?

1. Is it ethical for retailers to offer and strongly promote service contracts?
2. When should you purchase a service contract?
3. Why do retailers continue to offer these contracts, even under criticism from customer advocacy groups?

Video Case Wellbeing

In 2003, Dan Wales and Matt Lennox opened their first Wellbeing restaurant. Their goal was to offer consumers a healthy alternative to typical fast-food options. Working with fresh ingredients, bright and open stores, and a well-crafted, healthy menu, the new chain offered something new. "There are few truly healthy fast-food chains," says Wales. "People have been desperate for healthy options." So it came as no surprise that customers responded with enthusiasm to Wellbeing's new choices as they gobbled up sandwiches, salads, soups, juices, smoothies, and fruit salads. In only a few years, the chain has expanded to 18 stores and expects to nearly double that number in the next two years.

After viewing the video featuring Wellbeing, answer the following questions about retailing and wholesaling.

1. Categorize Wellbeing according to the four characteristics of retailers discussed in the chapter.
2. How is Wellbeing positioned in the marketplace? Which consumers does the chain target? Are its product assortment, pricing, promotion, and place decisions consistent with this targeting and positioning?
3. Which trend affecting the future of retailing do you think will most impact Wellbeing in the coming years?

Company Case Peapod: Thriving in the World of Online Groceries

After years of marketing consumer products for both Procter & Gamble and Kraft Foods, Andrew Parkinson was ready for a change. His brother Thomas, who owned a software company, was also ready for something new. The two decided to partner and enter the online grocery business. Given that the Internet grocery business has produced a high number of casualties, it may seem that venture was a suicide mission. But this case is very different from that of other online grocery companies. Andrew and Thomas Parkinson made their decision to start a company selling groceries online in 1989, years before the Internet and the World Wide Web would become available to the public. Today, not only is their company, Peapod LLC, still in business, it is the leader in online grocery retailing.

FROM IDEA TO REALITY

For decades, the retail grocery industry has been characterized by fierce competition, low margins, and powerful chains. In the late 1980s, most of these chains differentiated themselves based on price. But the Parkinson brothers perceived a niche that was not being satisfied by grocers. In the early 1900s, the most common way to purchase groceries was through a full-service neighborhood grocer. However, not since the industry made the shift to the more-familiar supermarket format has a grocery chain focused on differentiation through full service. The Parkinson brothers not only saw this as an opportunity, they wanted to take the service concept further than it had ever been taken. Their vision included giving customers the ability to place orders from their homes at any hour of the day, have the orders hand assembled and then have them delivered to customers' homes, even to be placed on the kitchen counter if desired.

Aspiring to succeed in the online grocery business in 1989 was indeed a pioneering venture. At that time, the general public had no concept of online communications. Peapod had to supply customers with a modem and software that would allow their home PCs to dial in and communicate with the company system. Given that most customers had never used a modem, they had to be taught how to do that as well. In the first few years of operations, Peapod focused exclusively on the metro Chicago area. Andrew and Thomas took care of all the aspects of running the business, from selling the service to packing orders and delivering them in their own cars.

From the beginning, Andrew and Thomas settled on a concept that would serve as the foundation for their business model: partnering with existing grocery chains. Rather than trying to tackle the challenges of online order fulfillment along with those of starting a freestanding grocery chain, it was clear to them that it would be better to serve as the order and delivery service for existing chains. In Chicago in the early 1990s, they partnered with Jewel Food Stores. As Peapod grew, they partnered with Safeway in San Francisco, Kroger in Columbus, and Stop & Shop in Boston. In 2001, Netherlands-based Royal Ahold, the parent company of Stop & Shop, purchased all existing shares of Peapod, making it a wholly owned subsidiary. This not only provided capital, it created a direct partnership with Stop & Shop and Giant, another Royal Ahold grocery chain on the east coast.

As of 2006, Peapod has delivered more than eight million orders to over 240,000 customers. It currently serves the Chicago area as well as east coast metropolitan markets where Stop & Shop and Giant have a presence. The online grocer assembles orders in one of two 75,000-square-foot warehouses, and in more than a dozen 7,500-square-foot "warerooms" located adjacent to partner stores. Although Peapod is far from providing service on a national level, the company covers 1,500 zip codes containing almost 13,000,000 households. Peapod has grown conservatively, yet it has averaged 25 percent annual revenue increases, a phenomenal feat in an industry characterized by single-digit growth rates.

PROVIDING CUSTOMER VALUE BY OVERCOMING NEGATIVE PERCEPTIONS

Customers most commonly cite convenience as their reason for purchasing groceries online. Many find the benefit of grocery shopping at any hour of the day from the comfort of home or the office very motivating. Yet many potential customers perceive numerous disadvantages that prevent them from ever trying online grocery services. The Parkinson brothers have always focused on providing customer value by addressing the following commonly perceived disadvantages.

Ordering on the Web is too complex and time consuming. Retail experts have widely recognized that the Internet is not well suited to shopping for and purchasing low-dollar, routinely purchased consumables. If it takes customers 30 minutes online to find the type and brand of bread, milk, cheese, and apples they want, they might as well just stop by the store on the way home from work.

The basic Peapod system requires an initial account setup that includes establishing a shopping list of commonly purchased items. Given that most people buy many of the same items regularly, this list becomes the basis for each order. The customer's core list is flexible to additions and deletions. As customers purchase new items, the Peapod system remembers those items and makes them available for future purchases without searching. Being able to quickly find an item through a keyword search can be much easier than trying to locate the same item in the aisles of a grocery store.

Finding new items is enhanced by Express Shop. This feature lets shoppers jot down an entire list and then provides matching products instantly. Any resulting products being compared can be sorted by price, nutritional content (sodium, fat, carbs, etc.), or even best-seller status. In a similar manner, shoppers can also personalize their lists around dietary needs or recipe requirements. To keep searching and browsing simple, Peapod offers a maximum of 8,000 items, as opposed to the 30,000 to 40,000 items available in the typical partner store.

People often do not know what they want until they browse the store. Even as customers go to the store with shopping lists, they often discover things as they walk the aisles. The Peapod Web site approximates in-store shopping by letting the customer browse for products in a traditional grocery store aisle format if they choose. Additionally, a "New Arrivals" icon highlights new products that customers might not think of before shopping. Shoppers can also easily find hundreds of weekly specials by clicking on the "Specials" tab, or by looking for red tags in normal browsing.

The quality of the delivered products might not be as good. The vast majority of food purchased in grocery stores is prepackaged. However, a commonly cited reason consumers give for not getting groceries online is that an unknown, unseen person will select their produce, meats, and bakery items. EMarketing analyst David Berkowitz says, "People who go in and feel fruit have no idea what they're doing, but it's still so important for them."

However, Peapod believes that it can do a better job of selecting foods and of transporting those foods in a way that maximizes quality. It trains order assemblers so that they know what to look for in a piece of produce. "I would pick your fruit the way I pick fruit for myself," said one trained shopper. Many customers don't stop to consider that the interior of a car on a hot summer day can wreak havoc on fresh produce, dairy products, and frozen foods. But Peapod equips its facilities and delivery vans with multiple climate-controlled zones, so the rotisserie chicken stays warm, the produce stays cool, and the ice cream stays rock hard.

Online groceries are too high priced. For the most part, Peapod's grocery prices match those found in partner stores. Peapod adds a modest flat fee that covers the cost of delivery: $6.95 for orders greater than $100 and $9.95 for orders between $50 and $100 (orders have a $50 minimum). Moreover, Peapod offers easily located "in-store" specials,

(case continues)

and drivers accept all manufacturer coupons and credits them to the next order.

Waiting to meet the delivery person is too inconvenient. When considering Peapod's delivery option, many potential customers envision spending hours "waiting for the cable installer." In actuality, customers can choose a two-hour delivery window that is convenient for them. What's more, they can place orders seven days a week, to be delivered as soon as the next day or as far as two weeks ahead. For people living in high-rise apartments, orders can be left with the doorman at any time.

THE COMPETITIVE LANDSCAPE

The first thing that comes to mind when most people think of online groceries is the string of high-profile dot-com failures of the late 1990s. The most notable failure was Webvan in California. Despite its grandiose predictions, the company burned through $830 million in venture capital and declared bankruptcy in 2001, without ever turning a profit. Experts now agree that Webvan grew too fast and took on too many of the aspects of the business without first establishing a foundation.

Whereas examples such as Webvan have left most people with the impression that the Internet grocery business failed completely, other companies have been slowly and quietly expanding. Peapod's growth model allowed the company not only to achieve operational stability prior to the dot-com blitz of online grocers but also to weather the storm and emerge strong and profitable. Since the dot-com bust, Peapod and others have gone quietly about their business. The current list of notable online grocers consists almost entirely of existing grocery chain companies that have ventured into the online sector. The list includes Safeway, Albertson's, Pathmark, Shoprite, Waldbaum's, Roche Bros., and Sam's Club. New York-based Freshdirect.com is the only other online grocer without a brick-and-mortar chain to have achieved a measurable level of success.

Each of these companies has rolled out services on a regional basis. The regions generally correspond to where chains have a brick-and-mortar presence. Companies are also wisely expanding in urban areas that are densely populated with potential customers that fit the profile. That profile is characterized by affluent, Internet-savvy, time-pressed consumers. This includes high-income households that are also two-paycheck or single-parent households. As a secondary market, people with physical disabilities are attracted to grocery delivery service.

Because the existing Internet grocers serve only select regional areas, they are often not in competition with each other. The most notable competitors of Peapod are Safeway in the Washington D.C./Baltimore area, Roche Bros. in Boston and Cape Cod, and Freshdirect.com in Westchester County, New York. These companies have many comparable features. But each company also has some points of differentiation. For example, Roche Bros. does not have a minimum order price, offers 20,000 items, and does not allow tipping (Peapod encourages it).

These points of differentiation don't concern Peapod much at this time. In any given market, Peapod faces at most one other formidable competitor. And although some experts have questioned whether or not a single metro area can support two major online grocers, Peapod believes that there is plenty of business to go around. Addressing the issue of competition, Peapod spokesperson Elana Margolis is more welcoming than concerned. "It validates the service. People are recognizing what we've realized all along, that people want options," she says. "It's a big enough market I think it can hold more than one grocery delivery business."

The industry is indeed growing. Whereas many local chains have experienced varying degrees of success with online sales, the major players are doing well. According to Jupiter Research analyst Patti Freeman Evans, online grocery sales reached $2.4 billion in 2004, just 0.4 percent of the total $570 billion grocery market. However, by 2008, overall online grocery sales are expected to hit $6.5 billion. Although that still represents only about 1 percent of the total market, it amounts to an annual growth rate of 42 percent, as much as 10 times that of the overall industry. Safeway expects that Internet sales could account for up to 5 percent of its total sales within a few years, without significant cannibalization.

If the past is any predictor of success, Peapod has a bright future. However, as overall sales for online grocers continue to grow, Peapod and its competitors will likely find emerging challenges. According to Claes Fornell, a professor of business at the University of Michigan, "more Internet shopping options have given consumers the upper hand in brick-and-mortar retail stores. [Consumers] are more powerful relative to the seller than they ever have been in the past. There is more pressure on the company to try to satisfy the customer." As Peapod continues to face the challenges of growing its business today, it will likely deal with a rising bar in the future.

Questions for Discussion

1. Visit www.Peapod.com and click on the "Groceries for your home" link. Enter a Chicago-area zip code (say 60602), and click on the "Learn More" arrow. Compare the Peapod customer experience to a brick-and-mortar grocery shopping experience. What benefits can a customer receive by using Peapod? What are the disadvantages?
2. Using the various characteristics for classifying types of retailers, develop a profile of Peapod.
3. Who does Peapod target? How does it position itself in this market? Does its marketing mix support this targeting and positioning?

4. Apply the wheel-of-retailing concept to the entire grocery industry, defining Peapod's role.
5. What does the future hold for Peapod, in both the short term and the long term?

Source: Steve Adams, "Fresh Rivalry," *The Patriot Ledger*, October 29, 2005, p. 37; Dina ElBoghdady, "Safeway Rolls Out Online Shopping," *Washington Post*, September 19, 2005, p. D01; Jen Haberkorn, "Going the Extra Smile," *Washington Times*, November 16, 2005; Bruce Mohl, "Like Peapod, Roche Bros. Now Aims to Deliver," *Boston Globe*, October 23, 2005, p. D1; Jason Straziuso, "After Flashy Failures, Online Groceries Quietly Grow," www.cnn.com, May 19, 2004; and Eileen Gunn, "Picking Up an Online Grocery Order," *Wall Street Journal*, April 6, 2006, p. D4. Also see "Company Information" at www.peapod.com/.