FACULTY OF BUSINESS, HUMANITIES & HOSPITALITY

MASTER IN BUSINESS ADMINISTRATION

BM4403

MARKETING MANAGEMENT

SELF INSTRUCTIONAL MATERIALS

ACADEMIC YEAR 2021

TABLE OF CONTENT

INTRODUCTION TO COURSE

Welcome to Marketing Management – Module BM4403.

This module, BM4403 presents the knowledge and understanding about the importance of marketing management in companies. It imparts the concepts and principles involved in marketing of the company's products and services and enabling the company to gain competitive position in the market.

The marketing function plays an important role in the sense that it is in contact with the external environment and acquires the necessary information for the development and improvement of the company's operations and processes in order to attain the stability with the environment. It is the only function that brings in the financial returns to the company for the continuous operations of the other functions to provide the support to the marketing function.

I truly hope that, like your predecessors, you will enjoy the module and find that our 'discussions' enhance your understanding of the marketing management process.

COURSE LEARNING OUTCOMES

After successful completion of this course, students should be able to:

- Apply the elements of marketing strategy and planning in designing a marketing plan for the organization.
- Evaluate the role of customer relationship management (CRM) in relation to competencies and capabilities of successful marketers.
- Utilize information to better understand competitors and customers.
- Demonstrate the use of appropriate marketing mix in conjunction with relationship marketing strategies to develop value offering in the marketplace.
- Demonstrate the ability to use various approaches to measure marketing performance.

SUPPORT AND CONTACT DETAILS

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COURSE ASSESSMENT

This module is assessed by both coursework and examination.
Coursework Percentage: 60%
Examination Percentage: 40%

Coursework Details:

TASKS	PERCENTAGE (%)
Forum	5
Quiz	15
Discussion	10
Journal Review	10
Individual Assignment	15
Presentation	5

Important Reminder:
You must submit the uploaded printout and originality report for each assignment from Turnitin system. The originality report must be less than 15%, otherwise it will be considered as failed script.

Final Exam (40%):
At the end of semester, students need to sit for the online final examination. The final exam questions consist of two sections. Section A consist of case study or short answer questions. Meanwhile, Section B consist of essay questions.

RECOMMENDED READING LISTS

Kotler, P., Keller, K. L., Ang, S. H., Leong, S. M., Tan, C. T. (2017). Marketing Management: An Asian Perspective. 7th edition. Singapore: Pearson.

Additional References:

- Kotler, P. & Keller, K. (2016). Marketing Management. 15th edition. New Jersey: Pearson/Prentice Hall.
- Kotler, P. & Armstrong, G. (2018). Principles of Marketing. 17th edition. New Jersey: Pearson/Prentice Hall.

LESSON 1: UNDERSTANDING MARKETING MANAGEMENT

LEARNING OUTCOMES

Upon the completion of the lessons, students should be able to:

1. Explain the role of marketing and its importance
2. Define marketing and marketing management
3. Describe the core concepts of marketing
4. Explain the marketing orientations of a firm
5. Describe the marketing management process

INTRODUCTION

Lesson 1 provides a detail illustration in understanding marketing management and why it is important. To prepare to be a marketer, you need to understand what is marketing is, how it works, who does it, and what is marketed. The first decade of the 21st century challenged firms to prosper financially and even survive in the face of an unforgiving economic environment. Marketing is playing a key role in addressing those challenges.

1.1 The Importance & Scope of Marketing

Marketing is about identifying and meeting human and social needs. One of the shortest good definitions of marketing is "meeting needs profitably." When eBay recognized that people were unable to locate some of the items they desired most, it created an online auction clearinghouse. When IKEA noticed that people wanted good furnishings at substantially lower prices, it created knockdown furniture. These two firms demonstrated marketing savvy and turned a private or social need into a profitable business opportunity.

What is Marketed?

1. **Goods** – Physical goods constitute the bulk of most countries' production and marketing efforts.
2. **Services** – Services include the work of airlines, hotels, car rental firms, barbers and beauticians, maintenance and repair people, and accountants, bankers, lawyers, engineers, doctors, software programmers, and management consultants. Many market offerings mix goods and services, such as a fast-food meal.
3. **Events** – Marketers promote time-based events, such as major trade shows, artistic performances, and company anniversaries. Global sporting events such as the Olympics and the World Cup are promoted aggressively to both companies and fans.
4. **Experiences** – By orchestrating several services and goods, a firm can create, stage, and market experiences.

5. **Persons** – By orchestrating several services and goods, a firm can create, stage, and market experiences.
6. **Places** – Cities, states, regions, and whole nations compete to attract tourists, residents, factories, and company headquarters.11 Place marketers include economic development specialists, real estate agents, commercial banks, local business associations, and advertising and public relations agencies.
7. **Properties** – Properties are intangible rights of ownership to either real property (real estate) or financial property (stocks and bonds). They are bought and sold, and these exchanges require marketing.
8. **Organizations** – Organizations work to build a strong, favorable, and unique image in the minds of their target publics.
9. **Information** – The production, packaging, and distribution of information are major industries.13 Information is essentially what books, schools, and universities produce, market, and distribute at a price to parents, students, and communities.
10. **Ideas** – Every market offering includes a basic idea. Charles Revson of Revlon once observed: "In the factory we make cosmetics; in the drugstore we sell hope." Products and services are platforms for delivering some idea or benefit.

Who Markets?

MARKETERS AND PROSPECTS – A marketer is someone who seeks a response—attention, a purchase, a vote, a donation—from another party, called the prospect. If two parties are seeking to sell something to each other, we call them both marketers.

Marketers are skilled at stimulating demand for their products, but that's a limited view of what they do. Just as production and logistics professionals are responsible for supply management, marketers are responsible for demand management. They seek to influence the level, timing, and composition of demand to meet the organization's objectives. Eight demand states are possible:

1. **Negative demand** – Consumers dislike the product and may even pay to avoid it.
2. **Nonexistent demand** – Consumers may be unaware of or uninterested in the product.
3. **Latent demand** – Consumers may share a strong need that cannot be satisfied by an existing product.
4. **Declining demand** – Consumers begin to buy the product less frequently or not at all.
5. **Irregular demand** – Consumer purchases vary on a seasonal, monthly, weekly, daily, or even hourly basis.
6. **Full demand** – Consumers are adequately buying all products put into the marketplace.
7. **Overfull demand** – More consumers would like to buy the product than can be satisfied.
8. **Unwholesome demand** – Consumers may be attracted to products that have undesirable social consequences.

MARKETS – Traditionally, a "market" was a physical place where buyers and sellers gathered to buy and sell goods. Economists describe a market as a collection of buyers and sellers who transact over a particular product or product class (such as the housing market or the grain market).

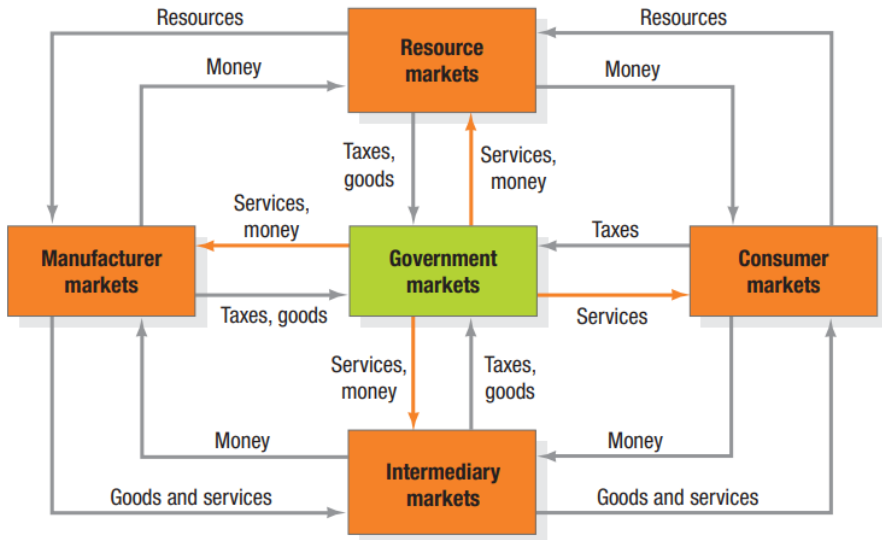

Figure 1.1: Structure of Flows in a Modern Exchange Economy

Five basic markets and their connecting flows are shown in Figure 1.1. Manufacturers go to resource markets (raw material markets, labor markets, money markets), buy resources and turn them into goods and services, and sell finished products to intermediaries, who sell them to consumers. Consumers sell their labor and receive money with which they pay for goods and services. The government collects tax revenues to buy goods from resource, manufacturer, and intermediary markets and uses these goods and services to provide public services. Each nation's economy, and the global economy, consists of interacting sets of markets linked through exchange processes.

Marketers use the term market to cover various groupings of customers. They view sellers as constituting the industry and buyers as constituting the market. They talk about need markets (the diet-seeking market), product markets (the shoe market), demographic markets (the youth market), and geographic markets (the Chinese market); or they extend the concept to cover voter markets, labor markets, and donor markets, for instance.

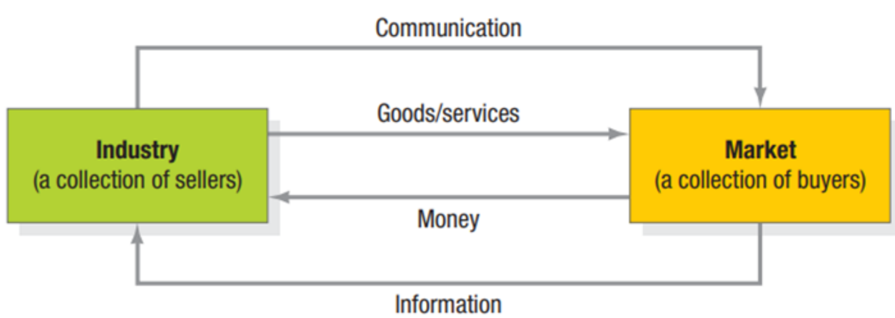

Figure 1.2: A Simple Marketing System

Figure 1.2 shows the relationship between the industry and the market. Sellers and buyers are connected by four flows. Sellers send goods and services and communications such as ads and direct mail to the market; in return they receive money and information such as customer attitudes and sales data. The inner loop shows an exchange of money for goods and services; the outer loop shows an exchange of information.

KEY CUSTOMER MARKETS – Consider the following key customer markets: consumer, business, global, and nonprofit.

Consumer Markets

Companies selling mass consumer goods and services such as juices, cosmetics, athletic shoes, and air travel spend a great deal of time establishing a strong brand image by developing a superior product and packaging, ensuring its availability, and backing it with engaging communications and reliable service.

Business Markets

Companies selling business goods and services often face well-informed professional buyers skilled at evaluating competitive offerings. Business buyers buy goods to make or resell a product to others at a profit. Business marketers must demonstrate how their products will help achieve higher revenue or lower costs. Advertising can play a role, but the sales force, the price, and the company's reputation may play a greater one.

Global Markets

Companies in the global marketplace must decide which countries to enter; how to enter each (as an exporter, licenser, joint venture partner, contract manufacturer, or solo manufacturer); how to adapt product and service features to each country; how to price products in different countries; and how to design communications for different cultures. They face different requirements for buying and disposing of property; cultural, language, legal and political differences; and currency fluctuations. Yet, the payoff can be huge.

Nonprofit and Governmental Markets

Companies selling to nonprofit organizations with limited purchasing power such as churches, universities, charitable organizations, and government agencies need to price carefully. Lower selling prices affect the features and quality the seller can build into the offering. Much government purchasing calls for bids, and buyers often focus on practical solutions and favor the lowest bid in the absence of extenuating factors.

1.2 The Core Marketing Concept

<u>What is Needs, Wants, and Demands?</u>

Needs are the basic human requirements such as for air, food, water, clothing, and shelter. Humans also have strong needs for recreation, education, and entertainment. These needs become **wants** when they are directed to specific objects that might satisfy the need. A U.S. consumer needs food but may want a Philly cheesesteak and an iced tea. A person in Afghanistan needs food but may want rice, lamb, and carrots. Wants are shaped by our society.

Demands are wants for specific products backed by an ability to pay. Many people want a Mercedes; only a few are able to buy one. Companies must measure not only how many people want their product, but also how many are willing and able to buy it.

Evolution of Earlier Marketing Ideas

The Production Concept
The production concept is one of the oldest concepts in business. It holds that consumers prefer products that are widely available and inexpensive. Managers of production-oriented businesses concentrate on achieving high production efficiency, low costs, and mass distribution. This orientation makes sense in developing countries such as China, where the largest PC manufacturer, Legend (principal owner of Lenovo Group), and domestic appliances giant Haier take advantage of the country's huge and inexpensive labor pool to dominate the market. Marketers also use the production concept when they want to expand the market.

The Product Concept
The product concept proposes that consumers favor products offering the most quality, performance, or innovative features. However, managers are sometimes caught in a love affair with their products. They might commit the "better-mousetrap" fallacy, believing a better product will by itself lead people to beat a path to their door. A new or improved product will not necessarily be successful unless it's priced, distributed, advertised, and sold properly.

The Selling Concept
The selling concept holds that consumers and businesses, if left alone, won't buy enough of the organization's products. It is practiced most aggressively with unsought goods—goods buyers don't normally think of buying such as insurance and cemetery plots—and when firms with overcapacity aim to sell what they make, rather than make what the market wants. Marketing based on hard selling is risky. It assumes customers coaxed into buying a product not only won't return or bad-mouth it or complain to consumer organizations but might even buy it again.

The Marketing Concept
The marketing concept emerged in the mid-1950s as a customer-centered, sense-and-respond philosophy. The job is to find not the right customers for your products, but the right products for your customers. Dell doesn't prepare a perfect computer for its target market. Rather, it provides product platforms on which each person customizes the features he or she desires in the computer. The marketing concept holds that the key to achieving organizational goals is being more effective than competitors in creating, delivering, and communicating superior customer value to your target markets.

The Holistic Marketing Concept
The holistic marketing concept is based on the development, design, and implementation of marketing programs, processes, and activities that recognize their breadth and interdependencies. Holistic marketing acknowledges that everything matters in marketing—and that a broad, integrated perspective is often necessary.

Holistic marketing thus recognizes and reconciles the scope and complexities of marketing activities. Figure 1.3 provides a schematic overview of four broad components characterizing holistic marketing: relationship marketing, integrated marketing, internal marketing, and performance marketing. We'll examine these major themes throughout this book. Successful companies keep their marketing changing with the changes in their marketplace—and marketspace.

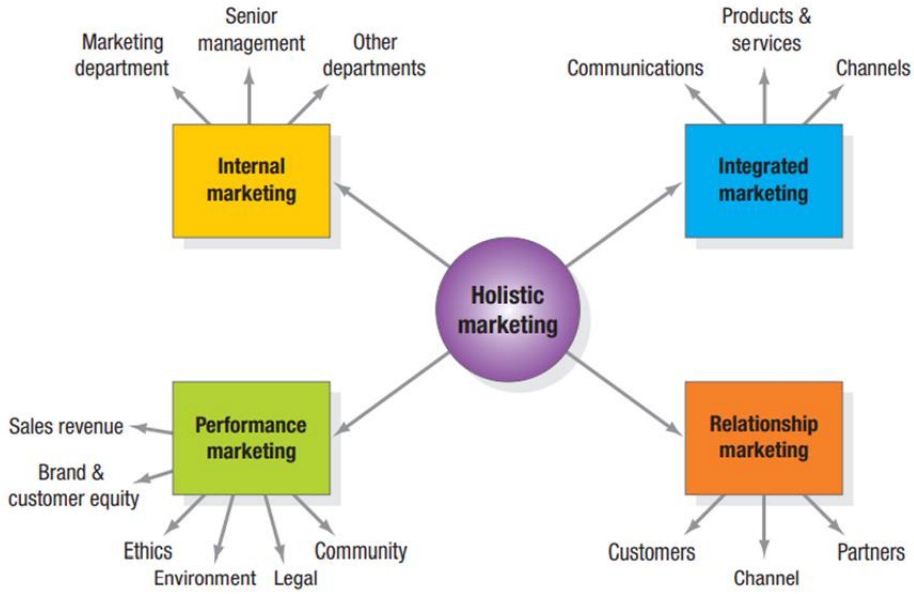

Figure 1.3: Holistic Marketing Dimensions

Updating the Four Ps

Given the breadth, complexity, and richness of marketing, however—as exemplified by holistic marketing—clearly these four Ps are not the whole story anymore. If we update them to reflect the holistic marketing concept, we arrive at a more representative set that encompasses modern marketing realities: people, processes, programs, and performance, as in Figure 1.5.

People reflects, in part, internal marketing and the fact that employees are critical to marketing success. Marketing will only be as good as the people inside the organization. It also reflects the fact that marketers must view consumers as people to understand their lives more broadly, and not just as they shop for and consume products and services.

Processes reflects all the creativity, discipline, and structure brought to marketing management. Marketers must avoid ad hoc planning and decision making and ensure that state-of-the-art marketing ideas and concepts play an appropriate role in all they do. Only by instituting the right set of processes to guide activities and programs can a firm engage in mutually beneficial long-term relationships. Another important set of processes guides the firm in imaginatively generating insights and breakthrough products, services, and marketing activities.

Programs reflects all the firm's consumer-directed activities. It encompasses the old four Ps as well as a range of other marketing activities that might not fit as neatly into the old view of marketing. Regardless of whether they are online or offline, traditional or nontraditional, these activities must be integrated such that their whole is greater than the sum of their parts and they accomplish multiple objectives for the firm.

Performance in holistic marketing; to capture the range of possible outcome measures that have financial and nonfinancial implications (profitability as well as brand and customer equity), and implications beyond the company itself (social responsibility, legal, ethical, and community related). Finally, these new four Ps actually apply to all disciplines within the company, and by thinking this way, managers grow more closely aligned with the rest of the company.

Figure 1.4: The Four P Components of the Marketing Mix

Figure 1.5: The Evolution of Marketing Management

POINTS TO PONDER

1. Marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders. Marketing management is the art and science of choosing

target markets and getting, keeping, and growing customers through creating, delivering, and communicating superior customer value.

2. Marketers are skilled at managing demand: they seek to influence its level, timing, and composition for goods, services, events, experiences, persons, places, properties, organizations, information, and ideas. They also operate in four different marketplaces: consumer, business, global, and nonprofit.
3. There are five competing concepts under which organizations can choose to conduct their business: the production concept, the product concept, the selling concept, the marketing concept, and the holistic marketing concept. The first three are of limited use today.
4. The holistic marketing concept is based on the development, design, and implementation of marketing programs, processes, and activities that recognize their breadth and interdependencies. Holistic marketing recognizes that everything matters in marketing and that a broad, integrated perspective is often necessary. Four components of holistic marketing are relationship marketing, integrated marketing, internal marketing, and socially responsible marketing.

SELF-CHECK

1. What is selling concept and how is it different than the marketing concept?
2. Given the marketing environment is highly competitive, discuss the marketing management orientations suitable for today's business firms
3. Outline the steps of the marketing management process that a marketing manager is responsible for.
4. Both value and satisfaction influence consumers' perception of a product worth. Yet, they are different. Discuss the statement.

REFERENCES

- Kotler, P. & Keller, K. (2016). Marketing Management. 15th edition. New Jersey: Pearson/Prentice Hall.
- Kotler, P., Keller, K. L., Ang, S. H., Leong, S. M., Tan, C. T. (2017). Marketing Management: An Asian Perspective. 7th edition. Singapore: Pearson.

LESSON 2: DEVELOPING MARKETING STRATEGIES AND PLANS

LEARNING OUTCOMES

Upon the completion of the lessons, students should be able to:

1. Explain the value chain and core competencies
2. Describe the role of strategic marketing planning
3. Explain the strategic marketing plan process

INTRODUCTION

Many marketers face challenging situations in meeting the needs of their customers as their competitors are trying to capture the interest of the same audience. Marketers must find ways to attract the attention of their target consumers amidst many market offerings from other competitors.

Consumers will choose a product that they perceive will give them the highest value. If they are satisfied with the product choice they have made, they may become loyal to the product and the marketer.

For many companies, the products involved are many, and the target markets are varied in various parts of the world. Therefore, the tasks involved to attract the various target markets for different products multi-fold and require proper planning.

2.1: Marketing and Customer Value

The Value Chain

Harvard's Michael Porter has proposed the value chain as a tool for identifying ways to create more customer value. According to this model, every firm is a synthesis of activities performed to design, produce, market, deliver, and support its product. The value chain identifies nine strategically relevant activities—five primary and four support activities—that create value and cost in a specific business.

The primary activities are (1) inbound logistics, or bringing materials into the business; (2) operations, or converting materials into final products; (3) outbound logistics, or shipping out final products; (4) marketing, which includes sales; and (5) service. Specialized departments handle the support activities— (1) procurement, (2) technology development, (3) human resource management, and (4) firm infrastructure. (Infrastructure covers the costs of general management, planning, finance, accounting, legal, and government affairs.)

The firm's task is to examine its costs and performance in each value-creating activity and look for ways to improve it. Managers should estimate competitors' costs and performances as benchmarks against which to compare their own.

The firm's success depends not only on how well each department performs its work, but also on how well the company coordinates departmental activities to conduct core business processes.
These processes include:

1. **The market-sensing process** – All the activities in gathering and acting upon information about the market
2. **The new-offering realization process** – All the activities in researching, developing, and launching new high-quality offerings quickly and within budget
3. **The customer acquisition process** – All the activities in defining target markets and prospecting for new customers
4. **The customer relationship management process** – All the activities in building deeper understanding, relationships, and offerings to individual customers
5. **The fulfillment management process** – All the activities in receiving and approving orders, shipping the goods on time, and collecting payment.

Core Competencies

A core competency has three characteristics: (1) It is a source of competitive advantage and makes a significant contribution to perceived customer benefits. (2) It has applications in a wide variety of markets. (3) It is difficult for competitors to imitate.

Competitive advantage also accrues to companies that possess distinctive capabilities or excellence in broader business processes. Competitive advantage ultimately derives from how well the company has fitted its core competencies and distinctive capabilities into tightly interlocking "activity systems." Competitors find it hard to imitate Southwest Airlines, Walmart, and IKEA because they are unable to copy their activity systems.

Business realignment may be necessary to maximize core competencies. It has three steps: (1) (re)defining the business concept or "big idea", (2) (re)shaping the business scope, and (3) (re)positioning the company's brand identity.

Holistic Marketing

Key management questions are:

1. **Value exploration** — How a company identifies new value opportunities?
2. **Value creation** — How a company efficiently creates more promising new value offerings?
3. **Value delivery** — How a company uses its capabilities and infrastructure to deliver the new value offerings more efficiently?

Holistic Marketing sees itself as integrating the value exploration, value creation, and value delivery activities with the purpose of building long-term, mutually satisfying relationships and co-prosperity among key stakeholders

The Central Role of Strategic Planning

To ensure they select and execute the right activities, marketers must give priority to strategic planning in three key areas: (1) managing a company's businesses as an investment portfolio, (2) assessing each business's strength by considering the market's growth rate and the company's position and fit in that market, and (3) establishing a strategy. The company must develop a game plan for achieving each business's long-run objectives.

Most large companies consist of four organizational levels: (1) corporate, (2) division, (3) business unit, and (4) product. Corporate headquarters is responsible for designing a corporate strategic plan to guide the whole enterprise; it makes decisions on the amount of resources to allocate to each division, as well as on which businesses to start or eliminate. Each division establishes a plan covering the allocation of funds to each business unit within the division. Each business unit develops a strategic plan to carry that business unit into a profitable future. Finally, each product level (product line, brand) develops a marketing plan for achieving its objectives.

The marketing plan is the central instrument for directing and coordinating the marketing effort. It operates at two levels: strategic and tactical. The strategic marketing plan lays out the target markets and the firm's value proposition, based on an analysis of the best market opportunities. The tactical marketing plan specifies the marketing tactics, including product features, promotion, merchandising, pricing, sales channels, and service. The complete planning, implementation, and control cycle of strategic planning is shown in Figure 2.1.

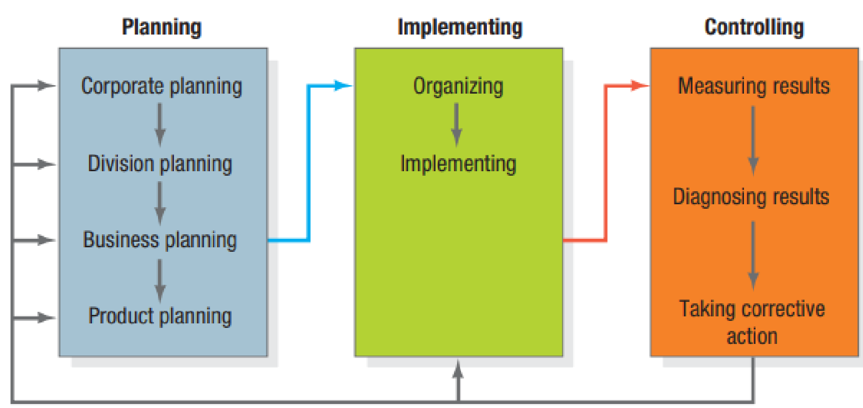

Figure 2.1: The Strategic Planning, Implementation, and Control Processes

2.2: Corporate and Division Strategic Planning

Some corporations give their business units freedom to set their own sales and profit goals and strategies. Others set goals for their business units but let them develop their own strategies. Still others set the goals and participate in developing individual business unit strategies.

All corporate headquarters undertake four planning activities: 1. Defining the corporate mission 2. Establishing strategic business units 3. Assigning resources to each strategic business unit 4. Assessing growth opportunities.

Defining the Corporate Mission

To define its mission, a company should address these classic questions: What is our business? Who is the customer? What is of value to the customer? What will our business be? What should our business be? These simple-sounding questions are among the most difficult a company will ever have to answer. Successful companies continuously raise and answer them.

Good mission statements have five major characteristics:

1. **They focus on a limited number of goals.** The statement "We want to produce the highestquality products, offer the most service, achieve the widest distribution, and sell at the lowest prices" claims too much.
2. **They stress the company's major policies and values**. They narrow the range of individual discretion so employees act consistently on important issues.
3. **They define the major competitive spheres within which the company will operate.**
4. **They take a long-term view**. Management should change the mission only when it ceases to be relevant.
5. **They are as short, memorable, and meaningful as possible.**

Establishing Strategic Business Units

A business can define itself in terms of three dimensions: customer groups, customer needs, and technology. Consider a small company that defines its business as designing incandescent lighting systems for television studios. Its customer group is television studios; the customer need is lighting; the technology is incandescent lighting. The company might want to expand to make lighting for homes, factories, and offices, or it could supply other services television studios need, such as heating, ventilation, or air conditioning. It could design other lighting technologies for television studios, such as infrared or ultraviolet lighting or perhaps environmentally friendly "green" fluorescent bulbs.

Dimensions that Define a Business:

1. Customer groups
2. Customer needs
3. Technology

Company	Product	Market
Missiouri-Pacific Railroad	We run a railroad	We are a people-and-goods mover
Xerox	We make copying equipment	We improve office productivity
Standard Oil	We sell gasoline	We supply energy
Columbia Pictures	We make movies	We entertain people

Table 1.0: Example for Product Orientation vs Market Orientation

Large companies normally manage quite different businesses, each requiring its own strategy. At one time, General Electric classified its businesses into 49 strategic business units (SBUs). The purpose of identifying the company's strategic business units is to develop separate strategies and assign appropriate funding. An SBU has three characteristics:

1. It is a single business, or a collection of related businesses, that can be planned separately from the rest of the company.
2. It has its own set of competitors.
3. It has a manager responsible for strategic planning and profit performance, who controls most of the factors affecting profit.

Assigning Resources to Each SBU

Once it has defined SBUs, management must decide how to allocate corporate resources to each. Several portfolio-planning models provide ways to make investment decisions. The GE/McKinsey Matrix classifies each SBU by the extent of its competitive advantage and the attractiveness of its industry. Management can decide to grow, “harvest” or draw cash from, or hold on to the business. Another model, BCG’s Growth-Share Matrix, uses relative market share and annual rate of market growth as criteria to make investment decisions, classifying SBUs as dogs, cash cows, question marks, and stars.

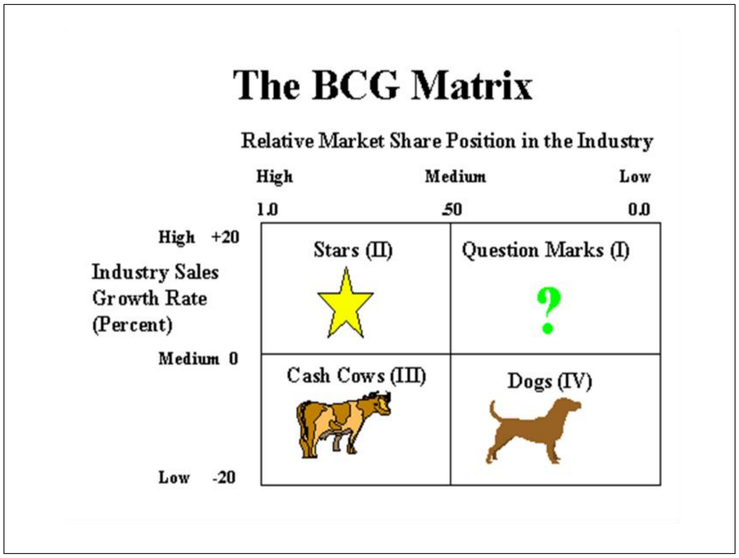

Figure 2.2: The BCG Matrix

Portfolio-planning models like these have fallen out of favor as oversimplified and subjective. Newer methods rely on shareholder value analysis, and on whether the market value of a company is greater with an SBU or without it (whether it is sold or spun off). These value calculations assess the potential of a business based on growth opportunities from global expansion, repositioning or retargeting, and strategic outsourcing

Assessing Growth Opportunities

Assessing growth opportunities includes planning new businesses, downsizing, and terminating older businesses. If there is a gap between future desired sales and projected sales, corporate management will need to develop or acquire new businesses to fill it.

Figure 2.3 illustrates this strategic-planning gap for a major manufacturer of blank compact disks called Musicale (name disguised). The lowest curve projects the expected sales over the next five years from the current business portfolio. The highest describes desired sales over the same period. Evidently, the company wants to grow much faster than its current businesses will permit. How can it fill the strategic-planning gap?

The first option is to identify opportunities for growth within current businesses (intensive opportunities). The second is to identify opportunities to build or acquire businesses related to current businesses (integrative opportunities). The third is to identify opportunities to add attractive unrelated businesses (diversification opportunities).

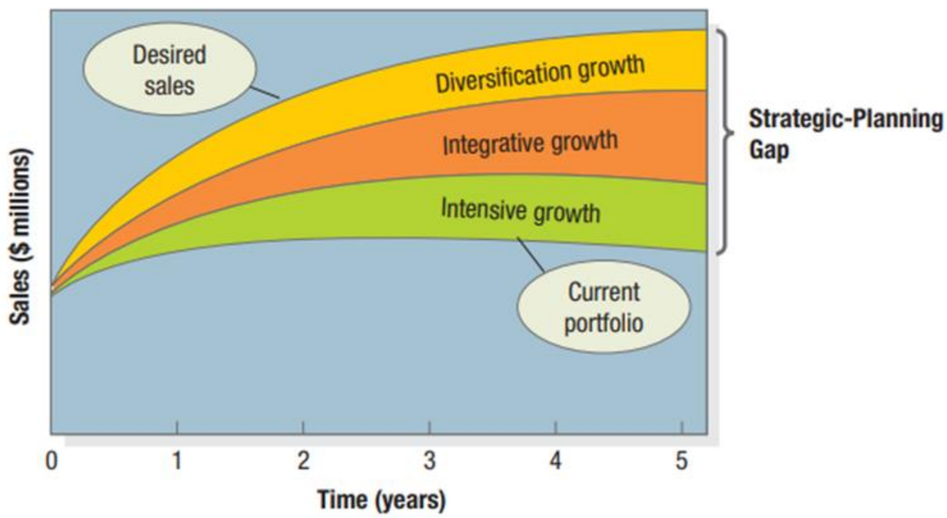

Figure 2.3: The Strategic-Planning Gap

Intensive Growth

Corporate management's first course of action should be a review of opportunities for improving existing businesses. One useful framework for detecting new intensivegrowth opportunities is a "product-market expansion grid." It considers the strategic growth opportunities for a firm in terms of current and new products and markets.

The company first considers whether it could gain more market share with its current products in their current markets, using a market-penetration strategy. Next it considers whether it can find or develop new markets for its current products, in a market-development strategy. Then it considers whether it can develop new products of potential interest to its current markets with a product-development strategy. Later the firm will also review opportunities to develop new products for new markets in a diversification strategy.

Integrative Growth

A business can increase sales and profits through backward, forward, or horizontal integration within its industry. Merck has gone beyond developing and selling prescription pharmaceuticals. It formed joint ventures in 1989 with Johnson & Johnson to sell over-the-counter pharmaceuticals; in 1991 with DuPont to expand basic research, and in 2000 with Schering-Plough to develop and market new prescription medicines. In 1997, Merck and Rhône-Poulenc S.A. (now Sanofi-Aventis S.A.) combined their animal health and poultry genetics businesses to form Merial Limited, a fully integrated animal health company. Finally, Merck purchased Medco, a mail-order pharmaceutical distributor, in 2003 and Sirna Therapeutics in 2006.

Horizontal mergers and alliances don't always work out. The merger between Sears and Kmart didn't solve either retailer's problems. Media companies, however, have long reaped the benefits of

integrative growth. Here's how one business writer explains the potential NBC could reap from its merger with Vivendi Universal Entertainment to become NBC Universal. Although it's a farfetched example, it gets across the possibilities inherent in this growth strategy:
"[When] the hit movie Fast & Furious 4 (produced by Universal Pictures) comes to television, it would air on Bravo (owned by NBC) or USA Network (owned by Universal), followed by the inevitable bid to make the movie into a TV series (by Universal Television Group), with the pilot being picked up by NBC. The show then begins airing on Hulu.com (owned in part by NBC), and ultimately leads to the creation of a popular amusement-park attraction at Universal Studios."

Diversification Growth

Diversification growth makes sense when good opportunities exist outside the present businesses—the industry is highly attractive and the company has the right mix of business strengths to succeed. From its origins as an animated film producer, The Walt Disney Company has moved into licensing characters for merchandised goods, publishing general interest fiction books under the Hyperion imprint, entering the broadcast industry with its own Disney Channel as well as ABC and ESPN, developing theme parks and vacation and resort properties, and offering cruise and commercial theatre experiences.

Downsizing and Divesting Older Business

Companies must carefully prune, harvest, or divest tired old businesses to release needed resources for other uses and reduce costs. To focus on its travel and credit card operations, American Express in 2005 spun off American Express Financial Advisors, which provided insurance, mutual funds, investment advice, and brokerage and asset management services (it was renamed Ameriprise Financial).

2.3: Business Unit Strategic Planning

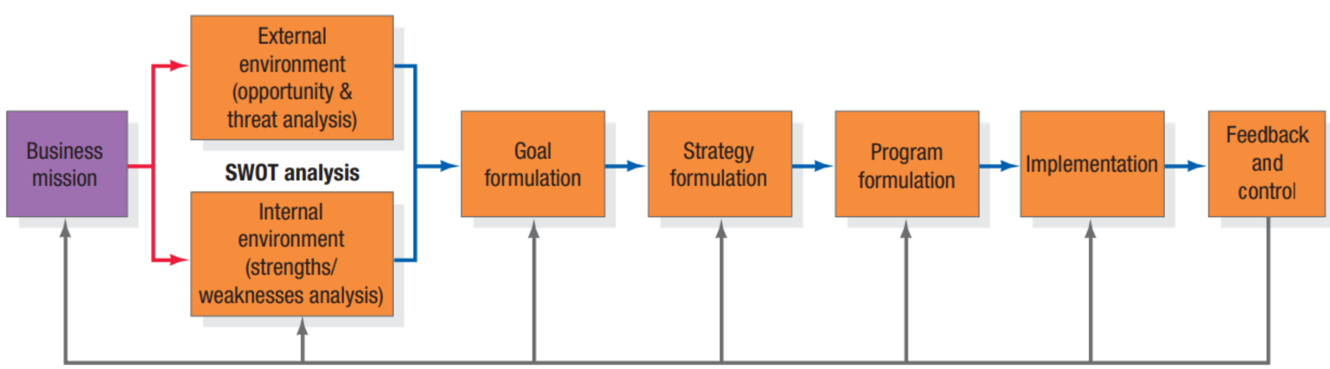

Figure 2.4: The Business Unit Strategic-Planning Process

Business Mission

Each business unit needs to define its specific **mission within** the broader company mission. Thus, a **television- studio-lighting-equipment** company might define its mission as, "To target major television studios and become their vendor of choice for lighting technologies that represent the most advanced and reliable studio lighting arrangements.

SWOT Analysis

The overall evaluation of a company's strengths, weaknesses, opportunities, and threats is called SWOT analysis. It's a way of monitoring the external and internal marketing environment

External Environment (Opportunity and Threat) Analysis

A business unit must monitor key macroenvironment forces and significant microenvironment factors that affect its ability to earn profits. It should set up a marketing intelligence system to track trends and important developments and any related opportunities and threats.

Good marketing is the art of finding, developing, and profiting from these opportunities. A marketing opportunity is an area of buyer need and interest that a company has a high probability of profitably satisfying.

Marketers need to be good at spotting opportunities. Consider the following:

1. ***A company may benefit from converging industry trends and introduce hybrid products or services that are new to the market.*** Major cell manufacturers have released phones with digital photo and video capabilities, and Global Positioning Systems (GPS).
2. ***A company may make a buying process more convenient or efficient***. Consumers can use the Internet to find more books than ever and search for the lowest price with a few clicks.
3. ***A company can meet the need for more information and advice***. Angie's List connects individuals with local home improvement contractors and doctors that have been reviewed by others.
4. ***A company can customize a product or service.*** Timberland allows customers to choose colors for different sections of their boots, add initials or numbers to their boots, and choose different stitching and embroidery.
5. ***A company can introduces a new capability***. Consumers can create and edit digital "iMovies" with the iMac and upload them to an Apple Web server or Web site such as YouTube to share with friends around the world.
6. ***A company may be able to deliver a product or service faster***. FedEx discovered a way to deliver mail and packages much more quickly than the U.S. Post Office.
7. ***A company may be able to offer a product at a much lower price.*** Pharmaceutical firms have created generic versions of brand-name drugs, and mail-order drug companies often sell for less.

To evaluate opportunities, companies can use market opportunity analysis (MOA) to ask questions like:

1. Can we articulate the benefits convincingly to a defined target market(s)?
2. Can we locate the target market(s) and reach them with cost-effective media and trade channels?
3. Does our company possess or have access to the critical capabilities and resources we need to deliver the customer benefits?
4. Can we deliver the benefits better than any actual or potential competitors?
5. Will the financial rate of return meet or exceed our required threshold for investment?

Internal Environment (Strengths and Weaknesses) Analysis

It's one thing to find attractive opportunities, and another to be able to take advantage of them. Each business needs to evaluate its internal strengths and weaknesses. Businesses can evaluate their own strengths and weaknesses by using a form, for example like the one shown in "Marketing Memo: Checklist for Performing Strengths/Weaknesses Analysis."

Clearly, the business doesn't have to correct all its weaknesses, nor should it gloat about all its strengths. The big question is whether it should limit itself to those opportunities for which it possesses the required strengths, or consider those that might require it to find or develop new strengths.

Goal Formulation

Once the company has performed a SWOT analysis, it can proceed to goal formulation, developing specific goals for the planning period. Goals are objectives that are specific with respect to magnitude and time. Most business units pursue a mix of objectives, including profitability, sales growth, market share improvement, risk containment, innovation, and reputation. The business unit sets these objectives and then manages by objectives (MBO). For an MBO system to work, the unit's objectives must meet four criteria:

1. Unit's objectives must be hierarchical
2. Objectives should be quantitative
3. Goals should be realistic
4. Objectives must be consistent

Strategic Formulation: Porter's Generic Strategies

Porter's Generic Strategies

Michael Porter has proposed three generic strategies that provide a good starting point for strategic thinking: overall cost leadership, differentiation, and focus.

Overall cost leadership. Firms work to achieve the lowest production and distribution costs so they can underprice competitors and win market share. They need less skill in marketing. The problem is that other firms will usually compete with still-lower costs and hurt the firm that rested its whole future on cost.

Differentiation. The business concentrates on achieving superior performance in an important customer benefit area valued by a large part of the market. The firm seeking quality leadership, for example, must make products with the best components, put them together expertly, inspect them carefully, and effectively communicate their quality.

Focus. The business focuses on one or more narrow market segments, gets to know them intimately, and pursues either cost leadership or differentiation within the target segment.

Strategic Formulation: Marketing Alliances

1. **Product or service alliances** — One company license another to produce its product, or two companies jointly market their complementary products or a new product.
2. **Promotional alliances** — One company agrees to carry a promotion for another company's product or service
3. **Logistics alliances** — One company offers logistical services for another company's product.
4. **Pricing collaborations** — One or more companies join in a special pricing collaboration.

2.4: The Nature and Contents of a Marketing Plan

A marketing plan is a written document that summarizes what the marketer has learned about the marketplace and indicates how the firm plans to reach its marketing objectives. It contains tactical guidelines for the marketing programs and financial allocations over the planning period.

A marketing plan is one of the most important outputs of the marketing process. It provides direction and focus for a brand, product, or company. Nonprofit organizations use marketing plans to guide their fund-raising and outreach efforts, and government agencies use them to build public awareness of nutrition and stimulate tourism.

A marketing plan usually contains the following sections:

1. **Executive summary and table of contents.** The marketing plan should open with a table of contents and brief summary for senior management of the main goals and recommendations.
2. **Situation analysis.** This section presents relevant background data on sales, costs, the market, competitors, and the various forces in the macroenvironment. How do we define the market, how big is it, and how fast is it growing? What are the relevant trends and critical issues? Firms will use all this information to carry out a SWOT analysis.
3. **Marketing strategy.** Here the marketing manager defines the mission, marketing and financial objectives, and needs the market offering is intended to satisfy as well as its competitive positioning. All this requires inputs from other areas, such as purchasing, manufacturing, sales, finance, and human resources.
4. **Financial projections.** Financial projections include a sales forecast, an expense forecast, and a break-even analysis. On the revenue side is forecasted sales volume by month and product category, and on the expense side the expected costs of marketing, broken down into finer categories. The break-even analysis estimates how many units the firm must sell monthly (or how many years it will take) to offset its monthly fixed costs and average per-unit variable costs. A more complex method of estimating profit is risk analysis. Here we obtain three estimates (optimistic, pessimistic, and most likely) for each uncertain variable affecting profitability, under an assumed marketing environment and marketing strategy for the planning period. The computer simulates possible outcomes and computes a distribution showing the range of possible rates of returns and their probabilities.
5. **Implementation controls.** The last section outlines the controls for monitoring and adjusting implementation of the plan. Typically, it spells out the goals and budget for each month or

quarter, so management can review each period's results and take corrective action as needed. Some organizations include contingency plans.

POINTS TO PONDER

1. The value delivery process includes choosing (or identifying), providing (or delivering), and communicating superior value. The value chain is a tool for identifying key activities that create value and costs in a specific business.
2. According to one view, holistic marketing maximizes value exploration by understanding the relationships between the customer's cognitive space, the company's competence space, and the collaborator's resource space; maximizes value creation by identifying new customer benefits from the customer's cognitive space, utilizing core competencies from its business domain, and selecting and managing business partners from its collaborative networks; and maximizes value delivery by becoming proficient at customer relationship management, internal resource management, and business partnership management.
3. Market-oriented strategic planning is the managerial process of developing and maintaining a viable fit between the organization's objectives, skills, and resources and its changing market opportunities. The aim of strategic planning is to shape the company's businesses and products so they yield target profits and growth. Strategic planning takes place at four levels: corporate, division, business unit, and product.
4. The corporate strategy establishes the framework within which the divisions and business units prepare their strategic plans. Setting a corporate strategy means defining the corporate mission, establishing strategic business units (SBUs), assigning resources to each, and assessing growth opportunities.
5. Strategic planning for individual businesses includes defining the business mission, analyzing external opportunities and threats, analyzing internal strengths and weaknesses, formulating goals, formulating strategy, formulating supporting programs, implementing the programs, and gathering feedback and exercising control.
6. Each product level within a business unit must develop a marketing plan for achieving its goals. The marketing plan is one of the most important outputs of the marketing process.

SELF CHECK

1. Defend or contradict this statement: Developing marketing strategy is more important than implementing marketing strategy because, if the strategy is flawed, its implementation doesn't matter.
2. In many organizations, marketing does not have a place of importance in the organizational hierarchy. Why do you think this happens? What are the consequences for a firm that gives little importance to marketing relative to other business functions?
3. What are some of the potential difficulties in approaching strategic planning from a balanced perspective? Isn't financial performance still the most important perspective to take in planning? Explain.

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LESSON 3: MARKETING RESEARCH

SYNOPSIS

Marketers have many important decisions to make throughout the marketing management process. When uncertain decisions are made, there will be risks involved. Uncertainties in marketing decisions can be reduced through marketing research. This lesson introduces marketing research, explains primary and secondary research, qualitative and quantitative research, and applies marketing research in market potential estimation and forecasting.

LEARNING OUTCOMES

Upon the completion of the lessons, students should be able to:
- Explain the role of marketing research in decision-making
- Describe the principal steps in research design
- Explain the characteristics of good marketing research
- Describe the methods of measuring and forecasting demand

3.0: THE MARKETING RESEARCH SYSTEM

Marketing managers often commission formal marketing studies of specific problems and opportunities. They may request a market survey, a product-preference test, a sales forecast by region, or an advertising evaluation. It's the job of the marketing researcher to produce insight into the customer's attitudes and buying behavior. Marketing insights provide diagnostic information about how and why we observe certain effects in the marketplace, and what that means to marketers.

Marketing research is the systematic design, collection, analysis, and reporting of data and findings relevant to a specific marketing situation facing the company. Marketing research, however, is not limited to large companies with big budgets and marketing research departments. Often at much smaller companies, everyone carries out marketing research— including the customers. Small companies can also hire the services of a marketing research firm or conduct research in creative and affordable ways, such as:

1. **Engaging students or professors to design and carry out projects**—Companies such as American Express, Booz Allen Hamilton, GE, Hilton Hotels, IBM, Mars, Price Chopper, and Whirlpool engage in "crowdcasting" and are sponsors of competitions such as the Innovation Challenge, where top MBA students compete in teams. The payoff to the students is experience and visibility; the payoff to the companies is a fresh set of eyes to solve problems at a fraction of what consultants would charge.
2. **Using the Internet**—A company can collect considerable information at very little cost by examining competitors' Web sites, monitoring chat rooms, and accessing published data.
3. **Checking out rivals**—Many small businesses, such as restaurants, hotels, or specialty retailers, routinely visit competitors to learn about changes they have made.

4. **Tapping into marketing partner expertise**—Marketing research firms, ad agencies, distributors, and other marketing partners may be able to share relevant market knowledge they have accumulated. Those partners targeting small or medium-sized businesses may be especially helpful. For example, to promote more shipping to China, UPS conducted several in-depth surveys of the Chinese market to portray its complexities but also its opportunities for even small and medium-sized businesses.

Most companies use a combination of marketing research resources to study their industries, competitors, audiences, and channel strategies. Companies normally budget marketing research at 1 percent to 2 percent of company sales and spend a large percentage of that on the services of outside firms. Marketing research firms fall into three categories:

1. **Syndicated-service research firms**—These firms gather consumer and trade information, which they sell for a fee. Examples include the Nielsen Company, Kantar Group, Westat, and IRI.
2. **Custom marketing research firms**—These firms are hired to carry out specific projects. They design the study and report the findings.
3. **Specialty-line marketing research firms**—These firms provide specialized research services. The best example is the field-service firm, which sells field interviewing services to other firms.

To take advantage of all these different resources and practices, good marketers adopt a formal marketing research process.

3.1: THE MARKETING RESEARCH PROCESS

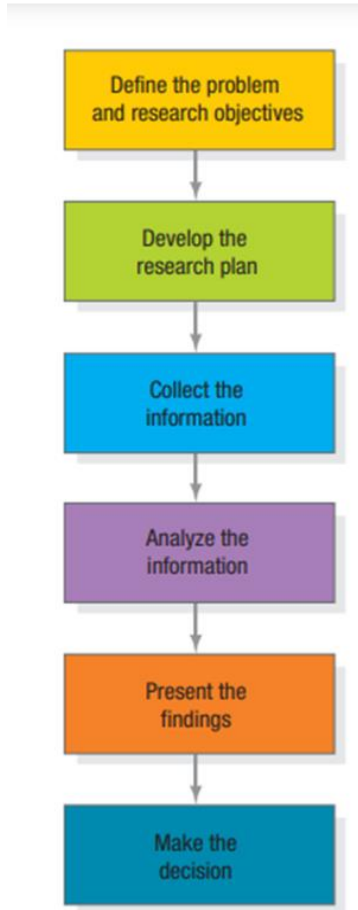

Figure 3.1: The Marketing Research Process

Step 1: Define the Problem, the Decision Alternatives, and the Research Objectives

Marketing managers must be careful not to define the problem too broadly or too narrowly for the marketing researcher. A marketing manager who says, "Find out everything you can about first-class air travelers' needs," will collect a lot of unnecessary information. One who says, "Find out whether enough passengers aboard a B747 flying direct between Chicago and Tokyo would be willing to pay $25 for an Internet connection for American Airlines to break even in one year on the cost of offering this service," is taking too narrow a view of the problem.

The marketing researcher might even ask, "Why does the Internet connection have to be priced at $25 as opposed to $15, $35, or some other price? Why does American have to break even on the cost of the service, especially if it attracts new customers?" Another relevant question to ask is, "How important is it to be first in the market, and how long can the company sustain its lead?"

The marketing manager and marketing researcher agreed to define the problem as follows: "Will offering an in-flight Internet service create enough incremental preference and profit for American

Airlines to justify its cost against other possible investments in service enhancements American might make?" To help in designing the research, management should first spell out the decisions it might face and then work backward. Suppose management outlines these decisions: (1) Should American offer an Internet connection? (2) If so, should we offer the service to first-class only, or include business class, and possibly economy class? (3) What price(s) should we charge? (4) On what types of planes and lengths of trips should we offer the service?

Now management and marketing researchers are ready to set specific research objectives: (1) What types of first-class passengers would respond most to using an in-flight Internet service? (2) How many first-class passengers are likely to use the Internet service at different price levels? (3) How many extra first-class passengers might choose American because of this new service? (4) How much long-term goodwill will this service add to American Airlines' image? (5) How important is Internet service to first-class passengers relative to other services, such as a power plug or enhanced entertainment?

Not all research projects can be this specific. Some research is exploratory—its goal is to shed light on the real nature of the problem and to suggest possible solutions or new ideas. Some research is descriptive—it seeks to quantify demand, such as how many first-class passengers would purchase in-flight Internet service at $25. Some research is causal—its purpose is to test a cause and-effect relationship

Step 2: Develop the Research Plan

The second stage of marketing research is where we develop the most efficient plan for gathering the needed information and what that will cost. To design a research plan, we need to make decisions about the data sources, research approaches, research instruments, sampling plan, and contact methods.

Data Sources

The researcher can gather secondary data, primary data, or both. Secondary data are data that were collected for another purpose and already exist somewhere. Primary data are data freshly gathered for a specific purpose or for a specific research project.

Research Approaches

Marketers collect primary data in five main ways: through observation, focus groups, surveys, behavioral data, and experiments.

Observational Research

Researchers can gather fresh data by observing the relevant actors and settings unobtrusively as they shop or consume products. Sometimes they equip consumers with pagers and instruct them to write down what they're doing whenever prompted, or they hold informal interview sessions at a café or bar. Photographs can also provide a wealth of detailed information.

Ethnographic research is a particular observational research approach that uses concepts and tools from anthropology and other social science disciplines to provide deep cultural understanding of how people live and work. The goal is to immerse the researcher into consumers' lives to uncover unarticulated desires that might not surface in any other form of research. Firms such as Fujitsu

Laboratories, Herman Miller, IBM, Intel, Steelcase, and Xerox have embraced ethnographic research to design breakthrough products.

Focus Group Research

A focus group is a gathering of 6 to 10 people carefully selected by researchers based on certain demographic, psychographic, or other considerations and brought together to discuss various topics of interest at length. Participants are normally paid a small sum for attending. A professional research moderator provides questions and probes based on the marketing managers' discussion guide or agenda. In focus groups, moderators try to discern consumers' real motivations and why they say and do certain things. They typically record the sessions, and marketing managers often remain behind two-way mirrors in the next room. To allow for more in-depth discussion with participants, focus groups are trending smaller in size.

Focus-group research is a useful exploratory step, but researchers must avoid generalizing from focus-group participants to the whole market, because the sample size is too small and the sample is not drawn randomly. Some marketers feel the research setting is too contrived and prefer to seek other means of collecting information that they believe are less artificial.

Survey Research

Companies undertake surveys to assess people's knowledge, beliefs, preferences, and satisfaction and to measure these magnitudes in the general population. A company such as American Airlines might prepare its own survey instrument to gather the information it needs, or it might add questions to an omnibus survey that carries the questions of several companies, at a much lower cost. It can also pose the questions to an ongoing consumer panel run by itself or another company. It may do a mall intercept study by having researchers approach people in a shopping mall and ask them questions.

Behavioral Research

Customers leave traces of their purchasing behavior in store scanning data, catalog purchases, and customer databases. Marketers can learn much by analyzing these data. Actual purchases reflect consumers' preferences and often are more reliable than statements they offer to market researchers. For example, grocery shopping data show that high income people don't necessarily buy the more expensive brands, contrary to what they might state in interviews; and many low-income people buy some expensive brands.

Experimental Research

The most scientifically valid research is experimental research, designed to capture cause-and-effect relationships by eliminating competing explanations of the observed findings. If the experiment is well designed and executed, research and marketing managers can have confidence in the conclusions. Experiments call for selecting matched groups of subjects, subjecting them to different treatments, controlling extraneous variables, and checking whether observed response differences are statistically significant.

Research Instruments

Marketing researchers have a choice of three main research instruments in collecting primary data: questionnaires, qualitative measures, and technological devices.

Questionnaires
A questionnaire consists of a set of questions presented to respondents. Because of its flexibility, it is by far the most common instrument used to collect primary data. Researchers need to carefully develop, test, and debug questionnaires before administering them on a large scale. The form, wording, and sequence of the questions can all influence the responses. Closed-end questions specify all the possible answers and provide answers that are easier to interpret and tabulate. Open-end questions allow respondents to answer in their own words and often reveal more about how people think. They are especially useful in exploratory research, where the researcher is looking for insight into how people think rather than measuring how many people think a certain way.

Qualitative Measures
Some marketers prefer more qualitative methods for gauging consumer opinion, because consumer actions don't always match their answers to survey questions. Qualitative research techniques are relatively unstructured measurement approaches that permit a range of possible responses. Their variety is limited only by the creativity of the marketing researcher.

Because of the freedom it affords both researchers in their probes and consumers in their responses, qualitative research can often be an especially useful first step in exploring consumers' brand and product perceptions. It is indirect in nature, so consumers may be less guarded and reveal more about themselves in the process.

Qualitative research does have its drawbacks. Marketers must temper the in-depth insights that emerge with the fact that the samples are often very small and may not necessarily generalize to broader populations. And different researchers examining the same qualitative results may draw very different conclusions.

<u>Sampling Plan</u>

After deciding on the research approach and instruments, the marketing researcher must design a sampling plan. This calls for three decisions:

1. **Sampling unit: Whom should we survey?** In the American Airlines survey, should the sampling unit consist only of first-class business travelers, first-class vacation travelers, or both? Should it include travelers under age 18? Both traveler and spouse? Once they have determined the sampling unit, marketers must develop a sampling frame so everyone in the target population has an equal or known chance of being sampled.
2. **Sample size: How many people should we survey?** Large samples give more reliable results, but it's not necessary to sample the entire target population to achieve reliable results. Samples of less than 1 percent of a population can often provide good reliability, with a credible sampling procedure.
3. **Sampling procedure: How should we choose the respondents?** Probability sampling allows marketers to calculate confidence limits for sampling error and makes the sample more representative. Thus, after choosing the sample, marketers could conclude that "the interval five to seven trips per year has 95 chances in 100 of containing the true number of trips taken annually by first-class passengers flying between Chicago and Tokyo.

<u>Contact Methods</u>

Mail Contacts: The mail questionnaire is one way to reach people who would not give personal interviews or whose responses might be biased or distorted by the interviewers. Mail questionnaires require simple and clearly worded questions. Unfortunately, the response rate is usually low or slow.

Telephone Contacts: Telephone interviewing is a good method for gathering information quickly; the interviewer is also able to clarify questions if respondents do not understand them. Interviews must be brief and not too personal.

Personal Contacts: Personal interviewing is the most versatile method. The interviewer can ask more questions and record additional observations about the respondent, such as dress and body language. At the same time, however, personal interviewing is the most expensive method, is subject to interviewer bias, and requires more administrative planning and supervision. Personal interviewing takes two forms. In arranged interviews, marketers contact respondents for an appointment and often offer a small payment or incentive. In intercept interviews, researchers stop people at a shopping mall or busy street corner and request an interview on the spot. Intercept interviews must be quick, and they run the risk of including nonprobability samples.

Online Contacts: An approach of increasing importance, the Internet offers many ways to do research. A company can embed a questionnaire on its Web site and offer an incentive to answer it, or it can place a banner on a frequently visited site such as Yahoo!, inviting people to answer some questions and possibly win a prize.

There are a number of pros and cons to online research.

Here are some advantages:

1. **Online research is inexpensive**. A typical e-mail survey can cost between 20 percent and 50 percent less than what a conventional survey costs, and return rates can be as high as 50 percent.
2. **Online research is fast**. Online surveys are fast because the survey can automatically direct respondents to applicable questions and transmit results immediately. One estimate says an online survey can generate 75 percent to 80 percent of the targeted response in 48 hours, compared to a telephone survey that can require 70 days to obtain 150 interviews.
3. **People tend to be honest and thoughtful online.** People may be more open about their opinions when they can respond privately and not to another person whom they feel might be judging them, especially on sensitive topics (such as, "how often do you bathe or shower?"). Because they choose when and where they take the survey and how much time to devote to each question, they may be more relaxed, introspective, and candid.
4. **Online research is versatile.** Increased broadband penetration offers online research even more flexibility and capabilities. For instance, virtual reality software lets visitors inspect 3-D models of products such as cameras, cars, and medical equipment and manipulate product characteristics. Even at the basic tactile level, online surveys can make answering a questionnaire easier and more fun than paper-and-pencil versions. Online community blogs allow customer participants to interact with each other.

Some disadvantages include:

1. **Samples can be small and skewed**. Some 40 percent of households were without broadband Internet access in the United States in 2009; the percentage is even higher among lower income groups, in rural areas, and in most parts of Asia, Latin America, and Central and Eastern Europe, where socioeconomic and education levels also differ. Although it's certain that more and more people will go online, online market researchers must find creative ways to reach population segments on the other side of the "digital divide." One option is to combine offline sources with online findings. Providing temporary Internet access at locations such as malls and recreation centers is another strategy. Some research firms use statistical models to fill in the gaps in market research left by offline consumer segments.
2. **Online panels and communities can suffer from excessive turnover.** Members may become bored with the company's efforts and flee. Or perhaps even worse, they may stay but only half-heartedly participate. Panel and community organizers are taking steps to address the quality of the panel and the data they provide by raising recruiting standards, downplaying incentives, and carefully monitoring participation and engagement levels. New features, events, and other activities must be constantly added to keep members interested and engaged.
3. **Online market research can suffer from technological problems and inconsistencies**. Problems can arise with online surveys because browser software varies. The Web designer's final product may look very different on the research subject's screen.

STEP 3: COLLECT THE INFORMATION

The data collection phase of marketing research is generally the most expensive and the most prone to error. Marketers may conduct surveys in homes, over the phone, via the Internet, or at a central interviewing location like a shopping mall. Four major problems arise in surveys. Some respondents will be away from home or otherwise inaccessible and must be contacted again or replaced. Other respondents will refuse to cooperate. Still others will give biased or dishonest answers. Finally, some interviewers will be biased or dishonest.

Internationally, one of the biggest obstacles to collecting information is the need to achieve consistency. Latin American respondents may be uncomfortable with the impersonal nature of the Internet and need interactive elements in a survey so they feel they're talking to a real person. Respondents in Asia, on the other hand, may feel more pressure to conform and may therefore not be as forthcoming in focus groups as online. Sometimes the solution may be as simple as ensuring the right language is used.

STEP 4: ANALYZE THE INFORMATION

The next-to-last step in the process is to extract findings by tabulating the data and developing summary measures. The researchers now compute averages and measures of dispersion for the major variables and apply some advanced statistical techniques and decision models in the hope of discovering additional findings. They may test different hypotheses and theories, applying sensitivity analysis to test assumptions and the strength of the conclusions

STEP 5: PRESENT THE FINDINGS

As the last step, the researcher presents findings relevant to the major marketing decisions facing management. Researchers increasingly are being asked to play a more proactive, consulting role in translating data and information into insights and recommendations.

They're also considering ways to present research findings in as understandable and compelling a fashion as possible. For example, "Marketing Insight: Bringing Marketing Research to Life with Personas" describes an approach that some researchers are using to maximize the impact of their consumer research findings.

The main survey findings for the American Airlines case showed that:

1. Passengers' chief reason for using in-flight Internet service would be to stay connected and receive and send e-mails. Some would also pass the time surfing the Web. This entertainment capability would require expensive broadband Internet access, but passengers stated they would be able to charge the cost and their companies would pay.
2. At $25, about 5 out of 10 first-class passengers would use Internet service during a flight; about 6 would use it at $15. Thus, a fee of $15 would produce less revenue ($90 = 6 x $15) than $25 ($125 = 5 x $25). Assuming the same flight takes place 365 days a year, American could collect $45,625 (= $125 x 365) annually. Given an investment of $90,000, it would take two years to break even.
3. Offering in-flight Internet service would strengthen the public's image of American Airlines as an innovative and progressive airline. American would gain some new passengers and customer goodwill.

STEP 6: MAKE THE DECISION

The American Airlines managers who commissioned the research need to weigh the evidence. If their confidence in the findings is low, they may decide against introducing the in-flight Internet service. If they are predisposed to launching the service, the findings support their inclination. They may even decide to study the issues further and do more research. The decision is theirs, but rigorously done research provides them with insight into the problem (see Table 3.0).

Some organizations use marketing decision support systems to help their marketing managers make better decisions. For example, MIT's John Little defines a marketing decision support system (MDSS) as a coordinated collection of data, systems, tools, and techniques, with supporting software and hardware, by which an organization gathers and interprets relevant information from business and environment and turns it into a basis for marketing action. Once a year, Marketing News lists hundreds of current marketing and sales software programs that assist in designing marketing research studies, segmenting markets, setting prices and advertising budgets, analyzing media, and planning sales force activity.

Method	Explanation
Scientific Method	Effective marketing research uses the principles of the scientific method: careful observation, formulation of hypotheses, prediction, and testing.
Research creativity	In an award-winning research study to reposition Cheetos snacks, researchers dressed up in a brand mascot Chester Cheetah suit and walked around the streets of San Francisco. The response the character encountered led to the realization that even adults loved the fun and playfulness of Cheetos. The resulting repositioning led to a double-digit sales increase despite a tough business environment
Multiple methods	Marketing researchers shy away from overreliance on any one method. They also recognize the value of using two or three methods to increase confidence in the results
Interdependence of models and data	Marketing researchers recognize that data are interpreted from underlying models that guide the type of information sought.
Value and cost of information	Marketing researchers show concern for estimating the value of information against its cost. Costs are typically easy to determine, but the value of research is harder to quantify. It depends on the reliability and validity of the findings and management's willingness to accept and act on those findings
Healthy skepticism	Marketing researchers show a healthy skepticism toward glib assumptions made by managers about how a market works. They are alert to the problems caused by "marketing myths."
Ethical marketing	Marketing research benefits both the sponsoring company and its customers. The misuse of marketing research can harm or annoy consumers, increasing resentment at what consumers regard as an invasion of their privacy or a disguised sales pitch.

Table 3.0: The Seven Characteristics of Good Marketing Research

3.3: MEASURING MARKETING PRODUCTIVITY

Two complementary approaches to measuring marketing productivity are: (1) marketing metrics to assess marketing effects and (2) marketing-mix modeling to estimate causal relationships and measure how marketing activity affects outcomes. Marketing dashboards are a structured way to disseminate the insights gleaned from these two approaches within the organization.

Marketing Metrics

Marketers employ a wide variety of measures to assess marketing effects. Marketing metrics is the set of measures that helps them quantify, compare, and interpret their marketing performance.

London Business School's Tim Ambler suggests that if firms think they are already measuring marketing performance adequately, they should ask themselves five questions:

1. Do you routinely research consumer behavior (retention, acquisition, usage) and why consumers behave that way (awareness, satisfaction, perceived quality)?
2. Do you routinely report the results of this research to the board in a format integrated with financial marketing metrics?
3. In those reports, do you compare the results with the levels previously forecasted in the business plans?

4. Do you also compare them with the levels achieved by your key competitor using the same indicators? Do you adjust short-term performance according to the change in your marketing-based asset(s)?

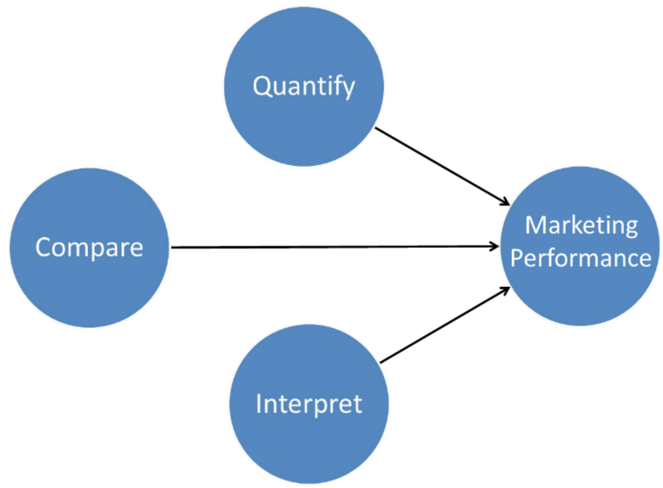

Figure 3.2: Marketing Metrics

I. External	II. Internal
Awareness	Awareness of goals
Market share (volume or value)	Commitment to goals
Relative price (market share value/volume)	Active innovation support
Number of complaints (level of dissatisfaction)	Resource adequacy
Consumer satisfaction	Staffing/skill levels
Distribution/availability	Desire to learn
Total number of customers	Willingness to change
Perceived quality/esteem	Freedom to fail
Loyalty/retention	Autonomy
Relative perceived quality	Relative employee satisfaction

Table 3.2: Sample Marketing Metrics

Marketing-Mix Model

Marketing-mix models analyze data from a variety of sources, such as retailer scanner data, company shipment data, pricing, media, and promotion spending data, to understand more precisely the effects of specific marketing activities.

To deepen understanding, marketers can conduct multivariate analyses, such as regression analysis, to sort through how each marketing element influences marketing outcomes such as brand sales or market share.

- Marketing-mix modeling focuses on incremental growth instead of baseline sales or long-term effects.
- The integration of important metrics such as customer satisfaction, awareness, and brand equity into marketing-mix modeling is limited.

Marketing Dashboards

Firms are also employing organizational processes and systems to make sure they maximize the value of all these different metrics. Management can assemble a summary set of relevant internal and external measures in a marketing dashboard for synthesis and interpretation. Marketing dashboards are like the instrument panel in a car or plane, visually displaying real-time indicators to ensure proper functioning. They are only as good as the information on which they're based, but sophisticated visualization tools are helping bring data alive to improve understanding and analysis.

- A **customer-performance scorecard** records how well the company is doing year after year on customer-based measures.
- A **stakeholder-performance scorecard** tracks the satisfaction of various constituencies who have a critical interest in and impact on the company's performance including employees, suppliers, banks, distributors, retailers, and stockholders.

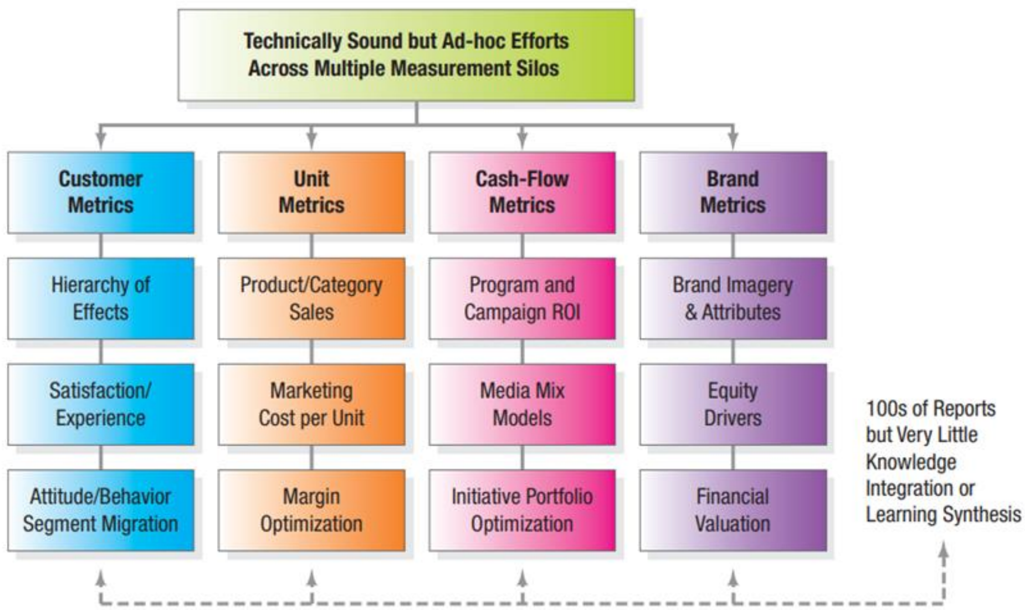

Figure 3.3: Marketing Measurement Pathway

Referring to Figure 3.3:

1. The ***customer metrics pathway*** looks at how prospects become customers, from awareness to preference to trial to repeat purchase, or some less linear model. This area also examines how the customer experience contributes to the perception of value and competitive advantage.
2. The ***unit metrics pathway*** reflects what marketers know about sales of product/service units—how much is sold by product line and/or by geography; the marketing cost per unit sold as an efficiency yardstick; and where and how margin is optimized in terms of characteristics of the product line or distribution channel.
3. The ***cash-flow metrics pathway*** focuses on how well marketing expenditures are achieving short-term returns. Program and campaign ROI models measure the immediate impact or net present value of profits expected from a given investment.

4. The ***brand metrics pathway*** tracks the development of the longer-term impact of marketing through brand equity measures that assess both the perceptual health of the brand from customer and prospective customer perspectives as well as the overall financial health of the brand.

POINTS TO PONDER

1. Companies can conduct their own marketing research or hire other companies to do it for them. Good marketing research is characterized by the scientific method, creativity, multiple research methods, accurate model building, cost-benefit analysis, healthy skepticism, and an ethical focus.
2. The marketing research process consists of defining the problem, decision alternatives; and research objectives; developing the research plan; collecting the information; analyzing the information; presenting the findings to management; and making the decision.
3. In conducting research, firms must decide whether to collect their own data or use data that already exist. They must also choose a research approach (observational, focus group, survey, behavioral data, or experimental) and research instruments (questionnaire, qualitative measures, or technological devices). In addition, they must decide on a sampling plan and contact methods (by mail, by phone, in person, or online).
4. Two complementary approaches to measuring marketing productivity are: (1) marketing metrics to assess marketing effects and (2) marketing-mix modeling to estimate causal relationships and measure how marketing activity affects outcomes. Marketing dashboards are a structured way to disseminate the insights gleaned from these two approaches within the organization.

SELF CHECK

1. Do you think the Internet has made it easier or more difficult to collect marketing data and information? Why? How might the major data collection issues of today compare to the issues that occurred in the pre-Internet era?
2. A marketing manager would like to ask his company's target market (a population) a few simple questions. If he wants to ensure every member of the population has an equal chance of being chosen for questioning, which sampling method should he use?
   He is also evaluating the best contact method to be used. His options are mail questionnaire, telephone interview, and personal interview. What is the main advantage of using each contact method?
3. You are hired as an external party to conduct marketing research for Nestle Malaysia to understand consumer behaviour in coffee consumption. Explain the research criteria needed to fulfil the research activities and produce quality research findings.

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LESSON 4: ANALYZING CONSUMER MARKETS

LEARNING OUTCOMES

Upon the completion of the lessons, students should be able to:

1. Explain the stimulus-response model of consumer behaviour
2. Describe the consumer characteristics that influence buying behaviour
3. Outline the psychological processes that influence consumer response to the marketing programme
4. Explain the consumer buying decision process

INTRODUCTION

The earlier lesson of marketing concept presented that firms should design an effective marketing mix that satisfies consumers. Thus, they need to investigate what, where, and how consumers make purchases. With the information, firms can better predict how consumers will react to their marketing strategies.

Firms must understand how consumers and organizations make decisions in purchasing products, as well as the roles they play in the buying decision. Firms must analyse why consumers make the purchases that they make, what factors influence their purchases, and what factors cause change in their opinion. The public can be initiators, influencers, deciders, buyers, or users. Marketing efforts should be targeted at each of these roles.

4.1: WHAT INFLUENCE CONSUMER BEHAVIOR

Consumer behavior is the study of how individuals, groups, and organizations select, buy, use, and dispose of goods, services, ideas, or experiences to satisfy their needs and wants. Marketers must fully understand both the theory and reality of consumer behavior.

A consumer's buying behavior is influenced by cultural, social, and personal factors. Of these, cultural factors exert the broadest and deepest influence.

Cultural Factors

Culture, subculture, and social class are particularly important influences on consumer buying behavior. Culture is the fundamental determinant of a person's wants and behavior. Through family and other key institutions, a child growing up in the United States is exposed to values such as achievement and success, activity, efficiency and practicality, progress, material comfort, individualism, freedom, external comfort, humanitarianism, and youthfulness. A child growing up in another country might have a different view of self, relationship to others, and rituals. Marketers must closely attend to cultural values in every country to understand how to best market their existing products and find opportunities for new products.

Each culture consists of smaller subcultures that provide more specific identification and socialization for their members. Subcultures include nationalities, religions, racial groups, and geographic regions. When subcultures grow large and affluent enough, companies often design specialized marketing programs to serve them.

Virtually all human societies exhibit social stratification, most often in the form of social classes, relatively homogeneous and enduring divisions in a society, hierarchically ordered and with members who share similar values, interests, and behavior. One classic depiction of social classes in the United States defined seven ascending levels: (1) lower lowers, (2) upper lowers, (3) working class, (4) middle class, (5) upper middles, (6) lower uppers, and (7) upper uppers.

Social class members show distinct product and brand preferences in many areas, including clothing, home furnishings, leisure activities, and automobiles. They also differ in media preferences; upper-class consumers often prefer magazines and books, and lower-class consumers often prefer television. Even within a category such as TV, upper-class consumers may show greater preference for news and drama, whereas lower-class consumers may lean toward reality shows and sports. There are also language differences—advertising copy and dialogue must ring true to the targeted social class.

<u>Social Factor</u>

In addition to cultural factors, social factors such as reference groups, family, and social roles and statuses affect our buying behavior.

Reference Groups – A person's reference groups are all the groups that have a direct (face to-face) or indirect influence on their attitudes or behavior. Groups having a direct influence are called membership groups. Some of these are primary groups with whom the person interacts fairly continuously and informally, such as family, friends, neighbors, and coworkers. People also belong to secondary groups, such as religious, professional, and trade-union groups, which tend to be more formal and require less continuous interaction.

Family – The family is the most important consumer buying organization in society, and family members constitute the most influential primary reference group. There are two families in the buyer's life. The family of orientation consists of parents and siblings. From parents a person acquires an orientation toward religion, politics, and economics and a sense of personal ambition, self-worth, and love.8 Even if the buyer no longer interacts very much with his or her parents, parental influence on behavior can be significant. Almost 40 percent of families have auto insurance with the same company as the husband's parents.

Roles and Status – We each participate in many groups—family, clubs, organizations. Groups often are an important source of information and help to define norms for behavior. We can define a person's position in each group in terms of role and status. A role consists of the activities a person is expected to perform. Each role in turn connotes a status. A senior vice president of marketing may be seen as having more status than a sales manager, and a sales manager may be seen as having more status than an office clerk. People choose products that reflect and communicate their role and their actual or desired status in society. Marketers must be aware of the status-symbol potential of products and brands

Personal Factors

Age and Stage in The Life Cycle – Our taste in food, clothes, furniture, and recreation is often related to our age. Consumption is also shaped by the family life cycle and the number, age, and gender of people in the household at any point in time. Marketers should also consider critical life events or transitions—marriage, childbirth, illness, relocation, divorce, first job, career change, retirement, death of a spouse—as giving rise to new needs. These should alert service providers—banks, lawyers, and marriage, employment, and bereavement counselors—to ways they can help. For example, the wedding industry attracts marketers of a whole host of products and services.

Occupation and Economic Circumstances – Occupation also influences consumption patterns. Marketers try to identify the occupational groups that have above-average interest in their products and services and even tailor products for certain occupational groups: Computer software companies, for example, design different products for brand managers, engineers, lawyers, and physicians.

Personality and Self-Concept – Each person has personality characteristics that influence his or her buying behavior. By personality, we mean a set of distinguishing human psychological traits that lead to relatively consistent and enduring responses to environmental stimuli (including buying behavior). We often describe personality in terms of such traits as self-confidence, dominance, autonomy, deference, sociability, defensiveness, and adaptability.

Lifestyle and Values – People from the same subculture, social class, and occupation may lead quite different lifestyles. A lifestyle is a person's pattern of living in the world as expressed in activities, interests, and opinions. It portrays the "whole person" interacting with his or her environment. Marketers search for relationships between their products and lifestyle groups. A computer manufacturer might find that most computer buyers are achievement-oriented and then aim the brand more clearly at the achiever lifestyle.

4.2: KEY PSYCHOLOGICAL PROCESSES

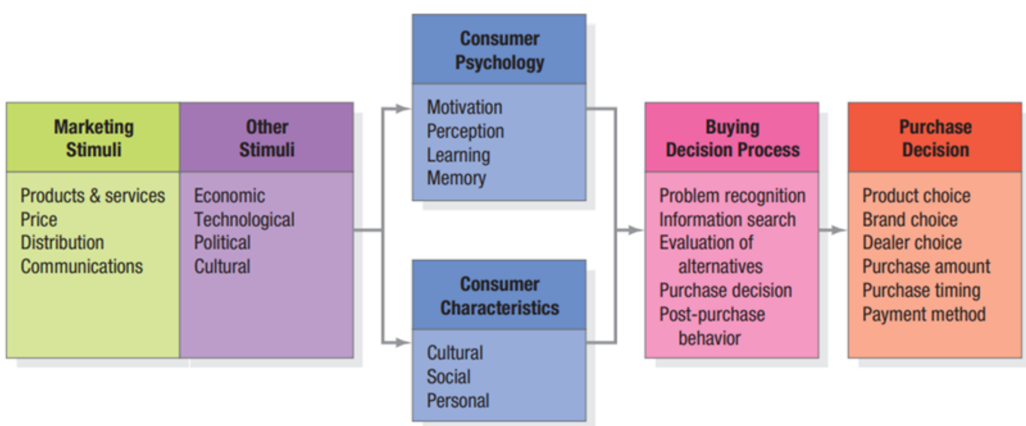

Figure 4.1: Model of Consumer Behavior

The starting point for understanding consumer behavior is the stimulus-response model shown in Figure 4.1. Marketing and environmental stimuli enter the consumer's consciousness, and a set of psychological processes combine with certain consumer characteristics to result in decision processes and purchase decisions. The marketer's task is to understand what happens in the consumer's consciousness between the arrival of the outside marketing stimuli and the ultimate purchase decisions. Four key psychological processes—motivation, perception, learning, and memory—fundamentally influence consumer responses

Motivation: Freud, Maslow, Herzberg

Three of the best-known theories of human motivation—those of Sigmund Freud, Abraham Maslow, and Frederick Herzberg—carry quite different implications for consumer analysis and marketing strategy.

Freud's Theory – Sigmund Freud assumed the psychological forces shaping people's behavior are largely unconscious, and that a person cannot fully understand his or her own motivations. Someone who examines specific brands will react not only to their stated capabilities, but also to other, less conscious cues such as shape, size, weight, material, color, and brand name. A technique called laddering lets us trace a person's motivations from the stated instrumental ones to the more terminal ones. Then the marketer can decide at what level to develop the message and appeal.

Maslow's Theory – Abraham Maslow sought to explain why people are driven by particular needs at particular times. His answer is that human needs are arranged in a hierarchy from most to least pressing—physiological needs, safety needs, social needs, esteem needs, and self-actualization needs (see Figure 4.2). People will try to satisfy their most important need first and then try to satisfy the next most important. For example, a starving man (need 1) will not take an interest in the latest happenings in the art world (need 5), nor in how he is viewed by others (need 3 or 4), nor even in whether he is breathing clean air (need 2), but when he has enough food and water, the next most important need will become salient.

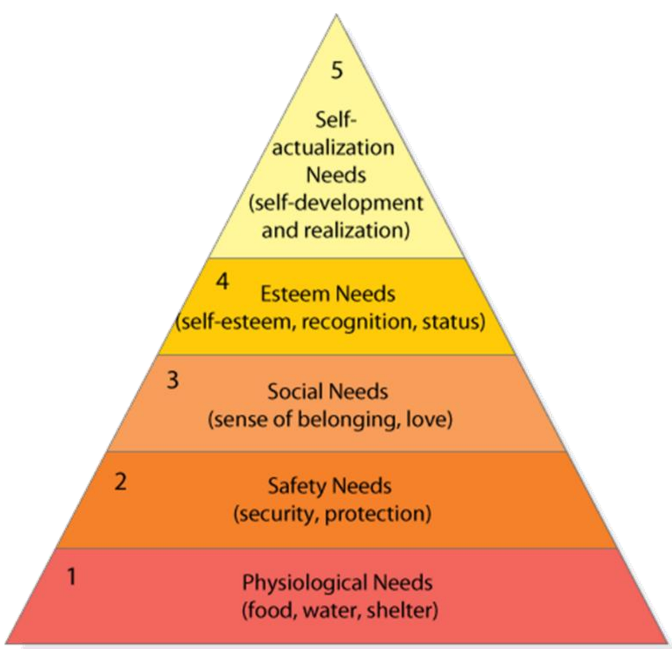

Figure 4.2: Maslow's Hierarchy of Needs

Herzberg's Theory – Frederick Herzberg developed a two-factor theory that distinguishes dissatisfiers (factors that cause dissatisfaction) from satisfiers (factors that cause satisfaction). The absence of dissatisfiers is not enough to motivate a purchase; satisfiers must be present. For example, a computer that does not come with a warranty would be a dissatisfier. Yet the presence of a product warranty would not act as a satisfier or motivator of a purchase, because it is not a source of intrinsic satisfaction. Ease of use would be a satisfier. Herzberg's theory has two implications. First, sellers should do their best to avoid dissatisfiers (for example, a poor training manual or a poor service policy). Although these things will not sell a product, they might easily unsell it. Second, the seller should identify the major satisfiers or motivators of purchase in the market and then supply them.

Perception

A motivated person is ready to act—how is influenced by his or her perception of the situation. In marketing, perceptions are more important than reality, because perceptions affect consumers' actual behavior. Perception is the process by which we select, organize, and interpret information inputs to create a meaningful picture of the world. It depends not only on physical stimuli, but also on the stimuli's relationship to the surrounding environment and on conditions within each of us. One person might perceive a fast-talking salesperson as aggressive and insincere; another, as intelligent and helpful. Each will respond to the salesperson differently.

People emerge with different perceptions of the same object because of three perceptual processes: selective attention, selective distortion, and selective retention.

Selective Attention – Attention is the allocation of processing capacity to some stimulus. Voluntary attention is something purposeful; involuntary attention is grabbed by someone or something.

1. **People are more likely to notice stimuli that relate to a current need.** A person who is motivated to buy a computer will notice computer ads and be less likely to notice DVD ads.
2. **People are more likely to notice stimuli they anticipate**. You are more likely to notice computers than radios in a computer store because you don't expect the store to carry radios.
3. **People are more likely to notice stimuli whose deviations are large in relationship to the normal size of the stimuli**. You are more likely to notice an ad offering $100 off the list price of a computer than one offering $5 off.

Selective Distortion – Even noticed stimuli don't always come across in the way the senders intended. Selective distortion is the tendency to interpret information in a way that fits our preconceptions. Consumers will often distort information to be consistent with prior brand and product beliefs and expectations.

Selective Retention – Most of us don't remember much of the information to which we're exposed, but we do retain information that supports our attitudes and beliefs. Because of selective retention, we're likely to remember good points about a product we like and forget good points about competing products. Selective retention again works to the advantage of strong brands. It also explains why marketers need to use repetition—to make sure their message is not overlooked.

Subliminal Perception – The selective perception mechanisms require consumers' active engagement and thought. A topic that has fascinated armchair marketers for ages is subliminal perception. They argue that marketers embed covert, subliminal messages in ads or packaging. Consumers are not consciously aware of them, yet they affect behavior. Although it's clear that mental processes include many subtle subconscious effects, no evidence supports the notion that marketers can systematically control consumers at that level, especially enough to change moderately important or strongly held beliefs.

Learning

Consumers learn through action. Learning describes changes in an individual's behavior arising from experience. Learning is a process that creates changes in behavior, immediate or expected, through experiences when it comes to choosing the right brand for their laptops.

Learning occurs faster and is retained longer. The more reinforcement that is received during learning, the more important the material to be learned.

Repetition in which advertising messages are spread over time, rather than clustered at one time in order to increase learning, is the key strategy in promotional campaigns.

Emotions

Consumer response is not all cognitive and rational; much may be emotional and invoke different kinds of feelings. A brand or product may make a consumer feel proud, excited, or confident. An ad may create feelings of amusement, disgust, or wonder.

Memory

Cognitive psychologists distinguish between short-term memory (STM)—a temporary and limited repository of information—and long-term memory (LTM)—a more permanent, essentially unlimited repository. All the information and experiences we encounter as we go through life can end up in our long-term memory.

Most widely accepted views of long-term memory structure assume we form some kind of associative model. For example, the associative network memory model views LTM as a set of nodes and links. Nodes are stored information connected by links that vary in strength. Any type of information can be stored in the memory network, including verbal, visual, abstract, and contextual.

A spreading activation process from node to node determines how much we retrieve and what information we can actually recall in any given situation. When a node becomes activated because we're encoding external information (when we read or hear a word or phrase) or retrieving internal information from LTM (when we think about some concept), other nodes are also activated if they're strongly enough associated with that node.

In this model, we can think of consumer brand knowledge as a node in memory with a variety of linked associations. The strength and organization of these associations will be important determinants of the information we can recall about the brand. Brand associations consist of all brand-related thoughts, feelings, perceptions, images, experiences, beliefs, attitudes, and so on that become linked to the brand node.

We can think of marketing as a way of making sure consumers have product and service experiences to create the right brand knowledge structures and maintain them in memory. Companies such as Procter & Gamble like to create mental maps of consumers that depict their knowledge of a particular brand in terms of the key associations likely to be triggered in a marketing setting, and their relative strength, favorability, and uniqueness to consumers. Figure 4.3 displays a very simple mental map highlighting brand beliefs for a hypothetical consumer for State Farm insurance.

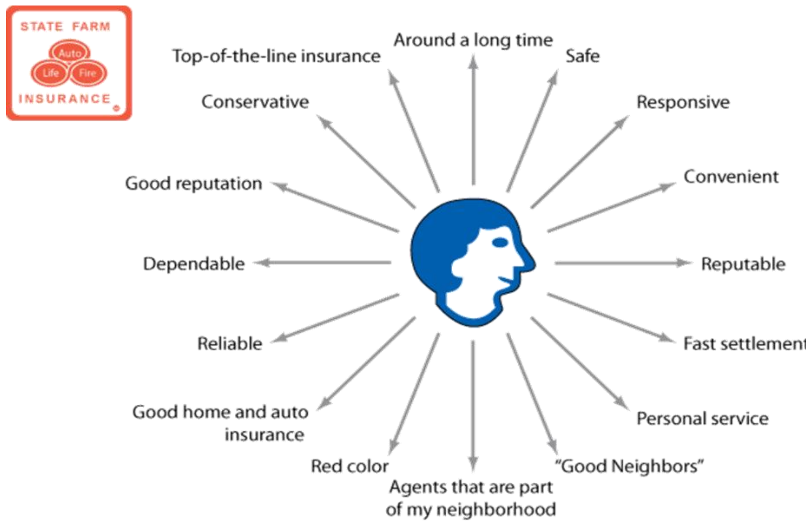

Figure 4.3: Hypothetical State Farm Mental Map

Memory Processes – Memory is a very constructive process, because we don't remember information and events completely and accurately. Often, we remember bits and pieces and fill in the rest based on whatever else we know. "Marketing Insight: Made to Stick" offers some practical tips for how marketers can ensure their ideas—inside or outside the company—are remembered and have impact.

Memory encoding describes how and where information gets into memory. The strength of the resulting association depends on how much we process the information at encoding (how much we think about it, for instance) and in what way. In general, the more attention we pay to the meaning of information during encoding, the stronger the resulting associations in memory will be.48 Advertising research in a field setting suggests that high levels of repetition for an uninvolving, unpersuasive ad, for example, are unlikely to have as much sales impact as lower levels of repetition for an involving, persuasive ad.

Memory retrieval is the way information gets out of memory. Three facts are important about memory retrieval.

1. The presence of other product information in memory can produce interference effects and cause us to either overlook or confuse new data. One marketing challenge in a category crowded with many competitors—for example, airlines, financial services, and insurance companies—is that consumers may mix up brands.
2. The time between exposure to information and encoding has been shown generally to produce only gradual decay. Cognitive psychologists believe memory is extremely durable, so once information becomes stored in memory, its strength of association decays very slowly.

3. Information may be available in memory but not be accessible for recall without the proper retrieval cues or reminders. The effectiveness of retrieval cues is one reason marketing inside a supermarket or any retail store is so critical—the actual product packaging, the use of in-store mini-billboard displays, and so on. The information they contain and the reminders they provide of advertising or other information already conveyed outside the store will be prime determinants of consumer decision making.

4.3: THE BUYING DECISION PROCESS – THE FIVE STAGE MODEL

Figure 4.4: The Buying Decision Process

Smart companies try to fully understand customers' buying decision process—all the experiences in learning, choosing, using, and even disposing of a product. Marketing scholars have developed a "stage model" of the process (see Figure 4.4). The consumer typically passes through five stages: problem recognition, information search, evaluation of alternatives, purchase decision, and post-purchase behavior. Clearly, the buying process starts long before the actual purchase and has consequences long afterward.

Consumers don't always pass through all five stages—they may skip or reverse some. When you buy your regular brand of toothpaste, you go directly from the need to the purchase decision, skipping information search and evaluation. The model in Figure 4.4 provides a good frame of reference, however, because it captures the full range of considerations that arise when a consumer faces a highly involving new purchase.

Problem Recognition

The buying process starts when the buyer recognizes a problem or need triggered by internal or external stimuli. With an internal stimulus, one of the person's normal needs—hunger, thirst, sex— rises to a threshold level and becomes a drive. A need can also be aroused by an external stimulus. A person may admire a friend's new car or see a television ad for a Hawaiian vacation, which inspires thoughts about the possibility of making a purchase.

Marketers need to identify the circumstances that trigger a particular need by gathering information from a number of consumers. They can then develop marketing strategies that spark consumer interest. Particularly for discretionary purchases such as luxury goods, vacation packages, and entertainment options, marketers may need to increase consumer motivation so a potential purchase gets serious consideration.

Information Search

Surprisingly, consumers often search for limited amounts of information. Surveys have shown that for durables, half of all consumers look at only one store, and only 30 percent look at more than one brand of appliances. We can distinguish between two levels of engagement in the search. The milder search state is called heightened attention. At this level a person simply becomes more receptive to information about a product. At the next level, the person may enter an active *information search*: looking for reading material, phoning friends, going online, and visiting stores to learn about the product.

Information Sources – Major information sources to which consumers will turn fall into four groups:

1. Personal: Family, friends, neighbors, acquaintances
2. Commercial: Advertising, Web sites, salespersons, dealers, packaging, displays
3. Public: Mass media, consumer-rating organizations
4. Experiential: Handling, examining, using the product

The relative amount and influence of these sources vary with the product category and the buyer's characteristics. Generally speaking, although consumers receive the greatest amount of information about a product from commercial—that is, marketer-dominated—sources, the most effective information often comes from personal or experiential sources, or public sources that are independent authorities.

Each source performs a different function in influencing the buying decision. Commercial sources normally perform an information function, whereas personal sources perform a legitimizing or evaluation function. For example, physicians often learn of new drugs from commercial sources but turn to other doctors for evaluations.

Search Dynamics – By gathering information, the consumer learns about competing brands and their features. The first box in Figure 4.5 shows the total set of brands available. The individual consumer will come to know a subset of these, the awareness set. Only some, the consideration set, will meet initial buying criteria. As the consumer gathers more information, just a few, the choice set, will remain strong contenders. The consumer makes a final choice from these.

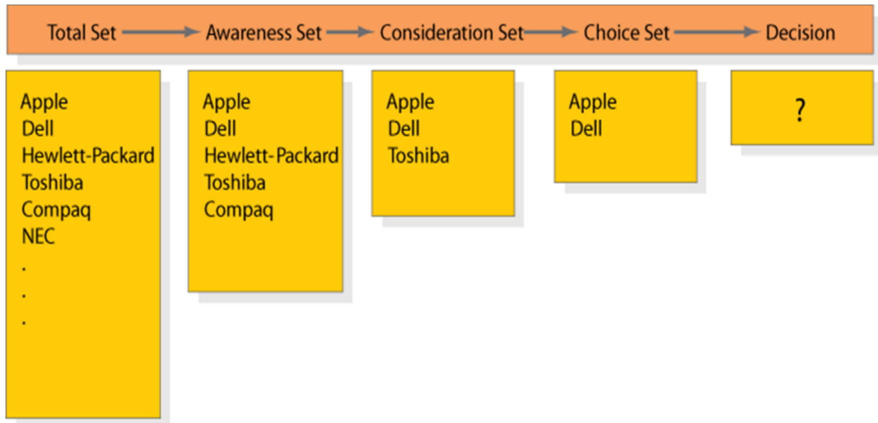

Figure 4.5: Successive Sets Involved in Consumer Decision Making

<u>Evaluation of Alternatives</u>

How does the consumer process competitive brand information and make a final value judgment? No single process is used by all consumers, or by one consumer in all buying situations. There are several processes, and the most current models see the consumer forming judgments largely on a conscious and rational basis.

Some basic concepts will help us understand consumer evaluation processes: First, the consumer is trying to satisfy a need. Second, the consumer is looking for certain benefits from the product solution. Third, the consumer sees each product as a bundle of attributes with varying abilities to deliver the benefits. The attributes of interest to buyers vary by product—for example:

1. **Hotels**—Location, cleanliness, atmosphere, price
2. **Mouthwash**—Color, effectiveness, germ-killing capacity, taste/flavor, price
3. **Tires**—Safety, tread life, ride quality, price

Consumers will pay the most attention to attributes that deliver the sought-after benefits. We can often segment the market for a product according to attributes and benefits important to different consumer groups.

Beliefs and Attitudes – Through experience and learning, people acquire beliefs and attitudes. These in turn influence buying behavior. A belief is a descriptive thought that a person holds about something. Just as important are attitudes, a person's enduring favorable or unfavorable evaluations, emotional feelings, and action tendencies toward some object or idea. People have attitudes toward almost everything: religion, politics, clothes, music, food.

Attitudes put us into a frame of mind: liking or disliking an object, moving toward or away from it. They lead us to behave in a fairly consistent way toward similar objects. Because attitudes economize on energy and thought, they can be very difficult to change. As a general rule, a company is well advised to fit its product into existing attitudes rather than try to change attitudes. If beliefs and attitudes become too negative, however, more serious steps may be necessary.

Expectancy-Value Model – The consumer arrives at attitudes toward various brands through an attribute evaluation procedure, developing a set of beliefs about where each brand stands on each attribute. The expectancy-value model of attitude formation posits that consumers evaluate products and services by combining their brand beliefs—the positives and negatives—according to importance.

Purchase Decision

In the evaluation stage, the consumer forms preferences among the brands in the choice set and may also form an intention to buy the most preferred brand. In executing a purchase intention, the consumer may make up to five sub-decisions: brand (brand A), dealer (dealer 2), quantity (one computer), timing (weekend), and payment method (credit card).

Non-compensatory Models of Consumer Choice – The expectancy-value model is a compensatory model, in that perceived good things about a product can help to overcome perceived bad things. But consumers often take "mental shortcuts" called heuristics or rules of thumb in the decision process.

With non-compensatory models of consumer choice, positive and negative attribute considerations don't necessarily net out. Evaluating attributes in isolation makes decision making easier for a consumer, but it also increases the likelihood that she would have made a different choice if she had deliberated in greater detail. We highlight three choice heuristics here:

1. Using the conjunctive heuristic, the consumer sets a minimum acceptable cutoff level for each attribute and chooses the first alternative that meets the minimum standard for all attributes.
2. With the lexicographic heuristic, the consumer chooses the best brand on the basis of its perceived most important attribute.
3. Using the elimination-by-aspects heuristic, the consumer compares brands on an attribute selected probabilistically—where the probability of choosing an attribute is positively related to its importance—and eliminates brands that do not meet minimum acceptable cutoffs.

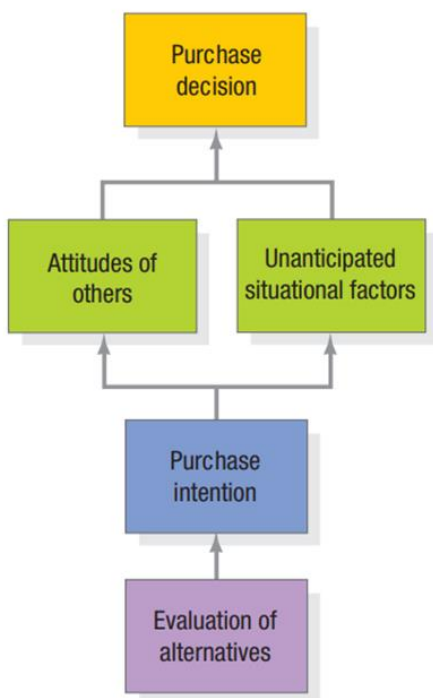

Figure 4.6: Steps between Evaluation of Alternatives and a Purchase Decision

Intervening Factors – Even if consumers form brand evaluations, two general factors can intervene between the purchase intention and the purchase decision (see Figure 6.6). The first factor is the attitudes of others. The influence of another person's attitude depends on two things: (1) the intensity of the other person's negative attitude toward our preferred alternative and (2) our motivation to comply with the other person's wishes.65 The more intense the other person's negativism and the closer he or she is to us, the more we will adjust our purchase intention. The converse is also true.

A consumer's decision to modify, postpone, or avoid a purchase decision is heavily influenced by one or more types of perceived risk:

1. Functional risk—The product does not perform to expectations.
2. Physical risk—The product poses a threat to the physical well-being or health of the user or others. Financial risk—The product is not worth the price paid.
3. Social risk—The product results in embarrassment in front of others.
4. Psychological risk—The product affects the mental well-being of the user.
5. Time risk—The failure of the product results in an opportunity cost of finding another satisfactory product.

The degree of perceived risk varies with the amount of money at stake, the amount of attribute uncertainty, and the level of consumer self-confidence. Consumers develop routines for reducing the uncertainty and negative consequences of risk, such as avoiding decisions, gathering information from friends, and developing preferences for national brand names and warranties. Marketers must understand the factors that provoke a feeling of risk in consumers and provide information and support to reduce it.

<u>**Post-purchase Behavior**</u>

Post-purchase Satisfaction – Satisfaction is a function of the closeness between expectations and the product's perceived performance. If performance falls short of expectations, the consumer is disappointed; if it meets expectations, the consumer is satisfied; if it exceeds expectations, the consumer is delighted. These feelings make a difference in whether the customer buys the product again and talks favorably or unfavorably about it to others.

The larger the gap between expectations and performance, the greater the dissatisfaction. Here the consumer's coping style comes into play. Some consumers magnify the gap when the product isn't perfect and are highly dissatisfied; others minimize it and are less dissatisfied.

Post-purchase Actions - A satisfied consumer is more likely to purchase the product again and will also tend to say good things about the brand to others. Dissatisfied consumers may abandon or return the product. They may seek information that confirms its high value. They may take public action by complaining to the company, going to a lawyer, or complaining to other groups (such as business, private, or government agencies). Private actions include deciding to stop buying the product (exit option) or warning friends (voice option).

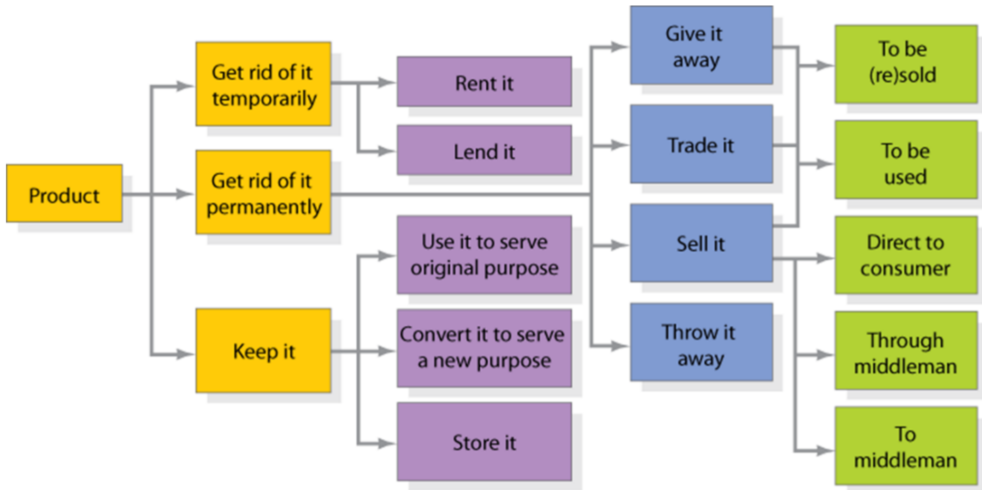

Figure 4.7: How Customers Use or Dispose of Products

Post-purchase Uses and Disposal – Marketers should also monitor how buyers use and dispose of the product (Figure 4.7). A key driver of sales frequency is product consumption rate—the more quickly buyers consume a product, the sooner they may be back in the market to repurchase it.
Consumers may fail to replace some products soon enough because they overestimate product life. One strategy to speed replacement is to tie the act of replacing the product to a certain holiday, event, or time of year.

For example, Oral B has tied toothbrush promotions to the springtime switch to daylight savings time. Another strategy is to provide consumers with better information about either (1) the time they first used the product or need to replace it or (2) its current level of performance. Batteries have built-in gauges that show how much power they have left; toothbrushes have color indicators to indicate when the bristles are worn; and so on. Perhaps the simplest way to increase usage is to learn when actual usage is lower than recommended and persuade customers that more regular usage has benefits, overcoming potential hurdles.

If consumers throw the product away, the marketer needs to know how they dispose of it, especially if—like batteries, beverage containers, electronic equipment, and disposable diapers—it can damage the environment.

POINTS TO PONDER

1. Consumer behavior is influenced by three factors: cultural (culture, subculture, and social class), social (reference groups, family, and social roles and statuses), and personal (age, stage in the life cycle, occupation, economic circumstances, lifestyle, personality, and self-concept). Research into these factors can provide clues to reach and serve consumers more effectively.
2. Four main psychological processes that affect consumer behavior are motivation, perception, learning, and memory.
3. To understand how consumers actually make buying decisions, marketers must identify who makes and has input into the buying decision; people can be initiators, influencers, deciders, buyers, or users. Different marketing campaigns might be targeted to each type of person.
4. The typical buying process consists of the following sequence of events: problem recognition, information search, evaluation of alternatives, purchase decision, and post-purchase behavior.

The marketers' job is to understand the behavior at each stage. The attitudes of others, unanticipated situational factors, and perceived risk may all affect the decision to buy, as will consumers' levels of post-purchase product satisfaction, use and disposal, and the company's actions.

5. Consumers are constructive decision makers and subject to many contextual influences. They often exhibit low involvement in their decisions, using many heuristics as a result.

SELF-CHECK

1. Considering the steps in the consumer buying process, describe how you (and your family) used this process to select your college. How many schools did you consider? How much time did you invest in this decision? When you were deciding on which college to attend, what objective and subjective criteria did you use in the alternative evaluation?
2. Discuss the situation where consumers' perception would influence their buying decision. Discuss what should be done by marketers for each situations.
3. Many people criticize marketing as being manipulative based on the argument that marketing activities create needs where none previously existed. Marketers of SUVs, tobacco products, diet programs, exercise equipment, and luxury products are typically the most criticized. Given what you now know about the differences between needs and wants, do you agree with these critics? Explain.

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LESSON 5: ANALYSING BUSINESS MARKETS

LEARNING OUTCOME

After studying this lesson, you should be able to:

1. Explain the categories of business buyers
2. Describe the business market and consumer market nature
3. Describe the participants in business buying process
4. Outline the business buying decision-making process

INTRODUCTION

This lesson will explore the type of organizations that make up the business market, their nature which is distinctive from the consumer market and the buying unit which exists in the business market. Furthermore, this lesson also will discuss the buying decision process which is more complex than the consumer's, the factors that influence business market buying behavior, and the types of buying behavior found in business market.

5.1: WHAT IS ORGANIZATIONAL BUYING?

Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services and identify, evaluate, and choose among alternative brands and suppliers.

The Business Market versus the Consumer Market

The business market consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others. The major industries making up the business market are agriculture, forestry, and fisheries; mining; manufacturing; construction; transportation; communication; public utilities; banking, finance, and insurance; distribution; and services.

Business marketers face many of the same challenges as consumer marketers. In particular, understanding their customers and what they value is of paramount importance to both. A survey of top business-to-business firms identified the following as challenges they faced:

1. Understanding deep customer needs in new ways;
2. Identifying new opportunities for organic business growth;
3. Improving value management techniques and tools;
4. Calculating better marketing performance and accountability metrics;
5. Competing and growing in global markets, particularly China;
6. Countering the threat of product and service commoditization by bringing innovative offerings to market faster and moving to more competitive business models; and
7. Convincing C-level executives to embrace the marketing concept and support robust marketing programs.

Business marketers contrast sharply with consumer markets in some ways, however:

Fewer, larger buyers: The business marketer normally deals with far fewer, much larger buyers than the consumer marketer does, particularly in such industries as aircraft engines and defense weapons.
Close supplier–customer relationship; Because of the smaller customer base and the importance and power of the larger customers, suppliers are frequently expected to customize their offerings to individual business customer needs.
Professional purchasing: Business goods are often purchased by trained purchasing agents, who must follow their organizations' purchasing policies, constraints, and requirements. Many of the buying instruments—for example, requests for quotations, proposals, and purchase contracts— are not typically found in consumer buying.
Multiple buying influences: More people typically influence business buying decisions. Buying committees consisting of technical experts and even senior management are common in the purchase of major goods. Business marketers need to send well-trained sales representatives and sales teams to deal with the well-trained buyers.
Multiple sales calls: A study by McGraw-Hill found that it took four to four and a half calls to close an average industrial sale. In the case of capital equipment sales for large projects, it may take many attempts to fund a project, and the sales cycle—between quoting a job and delivering the product—is often measured in years.
Derived demand: The demand for business goods is ultimately derived from the demand for consumer goods. For this reason, the business marketer must closely monitor the buying patterns of ultimate consumers.
Inelastic demand: The total demand for many business goods and services is inelastic—that is, not much affected by price changes. Shoe manufacturers are not going to buy much more leather if the price of leather falls, nor will they buy much less leather if the price rises unless they can find satisfactory substitutes.
Fluctuating demand: The demand for business goods and services tends to be more volatile than the demand for consumer goods and services. A given percentage increase in consumer demand can lead to a much larger percentage increase in the demand for plant and equipment necessary to produce the additional output.
Geographically concentrated buyers: At the same time, business marketers need to monitor regional shifts of certain industries.
Direct purchasing: Business buyers often buy directly from manufacturers rather than through intermediaries, especially items that are technically complex or expensive such as mainframes or aircraft.

Categories of Business Buyers

Producers	- Manufacturers and service providers - Purchase goods and services to produce other products, to incorporate into other products, or to support the day-to-day operations of the organization
Resellers	- Wholesalers and retailers - Resell products to other resellers or consumer at large
Government	- Federal, state and local municipalities - Provide service to the public

Institutions	- Non-profit organizations like universities, schools, hospitals, social clubs, etc. - Provide goods and services for people under their responsibilities e.g. students, patients, and patrons.

Table 5.0: Categories of Business Buyers

<u>**Buying Situations**</u>

The business buyer faces many decisions in making a purchase. How many depends on the complexity of the problem being solved, newness of the buying requirement, number of people involved, and time required. Three types of buying situations are the straight rebuy, modified rebuy, and new task.

Straight rebuy: In a straight rebuy, the purchasing department reorders supplies such as office supplies and bulk chemicals on a routine basis and chooses from suppliers on an approved list. The suppliers try to maintain product and service quality and often propose automatic reordering systems to save time. "Out-suppliers" attempt to offer something new or exploit dissatisfaction with a current supplier. Their goal is to get a small order and then enlarge their purchase share over time.

Modified rebuy: The buyer in a modified rebuy wants to change product specifications, prices, delivery requirements, or other terms. This usually requires additional participants on both sides. The in-suppliers become nervous and want to protect the account. The out-suppliers see an opportunity to propose a better offer to gain some business.

New task: A new-task purchaser buys a product or service for the first time (an office building, a new security system). The greater the cost or risk, the larger the number of participants, and the greater their information gathering—the longer the time to a decision.

5.2: PARTICIPANTS IN THE BUSINESS BUYING PROCESS

The buying center includes all members of the organization who play any of the following seven roles in the purchase decision process:

1. **Initiators**—Users or others in the organization who request that something be purchased.
2. **Users**—Those who will use the product or service. In many cases, the users initiate the buying proposal and help define the product requirements.
3. **Influencers**—People who influence the buying decision, often by helping define specifications and providing information for evaluating alternatives. Technical personnel are particularly important influencers.
4. **Deciders**—People who decide on product requirements or on suppliers.
5. **Approvers**—People who authorize the proposed actions of deciders or buyers.
6. **Buyers**—People who have formal authority to select the supplier and arrange the purchase terms. Buyers may help shape product specifications, but they play their major role in selecting vendors and negotiating. In more complex purchases, buyers might include high-level managers.

7. **Gatekeepers**—People who have the power to prevent sellers or information from reaching members of the buying center. For example, purchasing agents, receptionists, and telephone operators may prevent salespersons from contacting users or deciders.

5.3: STAGES IN THE BUSINESS BUYING PROCESS

Problem Recognition

The buying process begins when someone in the company recognizes a problem or need that can be met by acquiring a good or service. The recognition can be triggered by internal or external stimuli. The internal stimulus might be a decision to develop a new product that requires new equipment and materials, or a machine that breaks down and requires new parts. Or purchased material turns out to be unsatisfactory and the company searches for another supplier, or lower prices or better quality. Externally, the buyer may get new ideas at a trade show, see an ad, or receive a call from a sales representative who offers a better product or a lower price. Business marketers can stimulate problem recognition by direct mail, telemarketing, and calling on prospects.

General Need Description and Product Specification

Next, the buyer determines the needed item's general characteristics and required quantity. For standard items, this is simple. For complex items, the buyer will work with others—engineers, users—to define characteristics such as reliability, durability, or price. Business marketers can help by describing how their products meet or even exceed the buyer's needs.

The buying organization now develops the item's technical specifications. Often, the company will assign a product-value-analysis engineering team to the project. Product value analysis (PVA) is an approach to cost reduction that studies whether components can be redesigned or standardized or made by cheaper methods of production without adversely impacting product performance. The PVA team will identify overdesigned components, for instance, that last longer than the product itself. Tightly written specifications allow the buyer to refuse components that are too expensive or that fail to meet specified standards.

Supplier Search

The buyer next tries to identify the most appropriate suppliers through trade directories, contacts with other companies, trade advertisements, trade shows, and the Internet. The move to Internet purchasing has far-reaching implications for suppliers and will change the shape of purchasing for years to come. Companies that purchase over the Internet are utilizing electronic marketplaces in several forms:

Catalog sites – Companies can order thousands of items through electronic catalogs distributed by e-procurement software.

Vertical markets – Companies buying industrial products such as plastics, steel, or chemicals or services such as logistics or media can go to specialized Web sites (called e-hubs).

"Pure Play" auction sites – Ritchie Bros. Auctioneers for example, is the world's largest industrial auctioneer, with more than 40 auction sites worldwide. It sold $3.5 billion of used and unused equipment at more than 300 unreserved auctions in 2009, including a wide range of heavy equipment, trucks, and other assets for the construction, transportation, agricultural, material handling, mining, forestry, petroleum, and marine industries.

Barter markets – In barter markets, participants offer to trade goods or services.

Buying alliances – Several companies buying the same goods can join together to form purchasing consortia to gain deeper discounts on volume purchases.

E-Procurement

Web sites are organized around two types of e-hubs: vertical hubs centered on industries (plastics, steel, chemicals, paper) and functional hubs (logistics, media buying, advertising, energy management).

Lead Generation

The supplier's task is to ensure it is considered when customers are— or could be—in the market and searching for a supplier. Identifying good leads and converting them to sales requires the marketing and sales organizations to take a coordinated, multichannel approach to the role of trusted advisor to prospective customers. Marketing must work together with sales to define what makes a "sales ready" prospect and cooperate to send the right messages via sales calls, trade shows, online activities, PR, events, direct mail, and referrals.

Proposal Solicitation

The buyer next invites qualified suppliers to submit proposals. If the item is complex or expensive, the proposal will be written and detailed. After evaluating the proposals, the buyer will invite a few suppliers to make formal presentations.

Business marketers must be skilled in researching, writing, and presenting proposals. Written proposals should be marketing documents that describe value and benefits in customer terms. Oral presentations must inspire confidence and position the company's capabilities and resources so they stand out from the competition. Proposals and selling are often team efforts.

Supplier Selection

Before selecting a supplier, the buying center will specify and rank desired supplier attributes. The choice of attributes and their relative importance varies with the buying situation. Delivery reliability, price, and supplier reputation are important for routine-order products. For procedural-problem products, such as a copying machine, the three most important attributes are technical service, supplier flexibility, and product reliability. For political-problem products that stir rivalries in the organization (such as the choice of a computer system), the most important attributes are price, supplier reputation, product reliability, service reliability, and supplier flexibility.

Order-Routine Specification

After selecting suppliers, the buyer negotiates the final order, listing the technical specifications, the quantity needed, the expected time of delivery, return policies, warranties, and so on. Many industrial buyers lease heavy equipment such as machinery and trucks. The lessee gains a number of advantages: the latest products, better service, the conservation of capital, and some tax advantages. The lessor often ends up with a larger net income and the chance to sell to customers that could not afford outright purchase.

In the case of maintenance, repair, and operating items, buyers are moving toward blanket contracts rather than periodic purchase orders. A blanket contract establishes a long-term relationship in which the supplier promises to resupply the buyer as needed, at agreed-upon prices, over a specified period of time. Because the seller holds the stock, blanket contracts are sometimes called stockless purchase plans. The buyer's computer automatically sends an order to the seller when stock is needed. This system locks suppliers in tighter with the buyer and makes it difficult for out-suppliers to break in unless the buyer becomes dissatisfied with prices, quality, or service.

Companies that fear a shortage of key materials are willing to buy and hold large inventories. They will sign long-term contracts with suppliers to ensure a steady flow of materials. DuPont, Ford, and several other major companies regard long-term supply planning as a major responsibility of their purchasing managers. For example, General Motors wants to buy from fewer suppliers, who must be willing to locate close to its plants and produce high-quality components. Business marketers are also setting up extranets with important customers to facilitate and lower the cost of transactions. Customers enter orders that are automatically transmitted to the supplier.

Some companies go further and shift the ordering responsibility to their suppliers in systems called vendor-managed inventory (VMI). These suppliers are privy to the customer's inventory levels and take responsibility for replenishing automatically through continuous replenishment programs. For example, Plexco International AG supplies audio, lighting, and vision systems to the world's leading automakers. Its VMI program with its 40 suppliers resulted in significant time and cost savings and allowed the company to use former warehouse space for productive manufacturing activities.

Performance Review

The buyer periodically reviews the performance of the chosen supplier(s) using one of three methods. The buyer may contact end users and ask for their evaluations, rate the supplier on several criteria using a weighted-score method, or aggregate the cost of poor performance to come up with adjusted costs of purchase, including price. The performance review may lead the buyer to continue, modify, or end a supplier relationship.

Many companies have set up incentive systems to reward purchasing managers for good buying performance, in much the same way sales personnel receive bonuses for good selling performance. These systems lead purchasing managers to increase pressure on sellers for the best terms.

POINTS TO PONDER

1. Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services, then identify, evaluate, and choose among alternative brands and suppliers. The business market consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others.
2. Compared to consumer markets, business markets generally have fewer and larger buyers, a closer customer supplier relationship, and more geographically concentrated buyers. Demand in the business market is derived from demand in the consumer market and fluctuates with the business cycle. Nonetheless, the total demand for many business goods and services is quite price inelastic. Business marketers need to be aware of the role of professional purchasers and

their influencers, the need for multiple sales calls, and the importance of direct purchasing, reciprocity, and leasing.

3. The buying center is the decision-making unit of a buying organization. It consists of initiators, users, influencers, deciders, approvers, buyers, and gatekeepers. To influence these parties, marketers must be aware of environmental, organizational, interpersonal, and individual factors.
4. The buying process consists of eight stages called buy-phases: (1) problem recognition, (2) general need description, (3) product specification, (4) supplier search, (5) proposal solicitation, (6) supplier selection, (7) orderroutine specification, and (8) performance review.

SELF-CHECK

1. "Dealing with the business market is difficult. Understanding their customers is as important as understanding the business buyers' themselves". Discuss this statement.
2. "The business market differs from the consumers market because of the type of products that they purchase that are different". Comment on the statement.
3. The decision-making unit of a buying organization is usually known as the "buying centre". What is the consumption of the buying centre? List the buying process of an organization and briefly explain if it is similar to the consumer buying process.

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LESSON 6: MARKET SEGMENTATION, AND TARGETING

LEARNING OUTCOMES

After studying this lesson, you should be able to:

1. Explain the principles of market segmentation and the segmenting-targeting-positioning process
2. Enumerate the characteristics and differences between market segmentation and product differentiation
3. Discuss the market segmentation strategies for both consumer and business-to business markets
4. Explain the requirements for effective segmentation
5. Describe the different targeting strategies
6. Explain the concept of positioning
7. Explain the use of perceptual maps in the positioning process

INTRODUCTION

Due to constraints and limitations to serve an entire market population, most firms pursue target marketing where they concentrate their effort on certain fragments of the market. This is known as market segmentation which is an important part of marketing strategy. The entire market is subdivided into various segments through a process that is referred to as the segmenting-targeting-positioning (STP) process. The three activities – segmenting, targeting and positioning – are normally commenced in sequence, and this lesson is structured around these key elements.

6.1: BASES FOR SEGMENTING CONSUMER MARKETS

Market segmentation divides a market into well-defined slices. A market segment consists of a group of customers who share a similar set of needs and wants. The marketer's task is to identify the appropriate number and nature of market segments and decide which one(s) to target.

The major segmentation variables—geographic, demographic, psychographic, and behavioral segmentation.

<u>Geographic Segmentation</u>

Geographic segmentation divides the market into geographical units such as nations, states, regions, counties, cities, or neighborhoods. The company can operate in one or a few areas, or it can operate in all but pay attention to local variations. In that way it can tailor marketing programs to the needs and wants of local customer groups in trading areas, neighborhoods, even individual stores. In a growing trend called grassroots marketing, such activities concentrate on getting as close and personally relevant to individual customers as possible.

Demographic Segmentation

In demographic segmentation, we divide the market on variables such as age, family size, family life cycle, gender, income, occupation, education, religion, race, generation, nationality, and social class. One reason demographic variables are so popular with marketers is that they're often associated with consumer needs and wants. Another is that they're easy to measure. Even when we describe the target market in non-demographic terms (say, by personality type), we may need the link back to demographic characteristics in order to estimate the size of the market and the media we should use to reach it efficiently.

Age and Life-Cycle Stage – Consumer wants and abilities change with age. Toothpaste brands such as Crest and Colgate offer three main lines of products to target kids, adults, and older consumers. Age segmentation can be even more refined. Pampers divides its market into prenatal, new baby (0–5 months), baby (6–12 months), toddler (13–23 months), and preschooler (24 months+).

Life Stage – People in the same part of the life cycle may still differ in their life stage. Life stage defines a person's major concern, such as going through a divorce, going into a second marriage, taking care of an older parent, deciding to cohabit with another person, deciding to buy a new home, and so on. These life stages present opportunities for marketers who can help people cope with their major concerns.

Gender – Men and women have different attitudes and behave differently, based partly on genetic makeup and partly on socialization. Women tend to be more communal-minded and men more self-expressive and goal-directed; women tend to take in more of the data in their immediate environment and men to focus on the part of the environment that helps them achieve a goal. A research study examining how men and women shop found that men often need to be invited to touch a product, whereas women are likely to pick it up without prompting. Men often like to read product information; women may relate to a product on a more personal level.

Income – Income segmentation is a long-standing practice in such categories as automobiles, clothing, cosmetics, financial services, and travel. However, income does not always predict the best customers for a given product. Blue-collar workers were among the first purchasers of color television sets; it was cheaper for them to buy these sets than to go to movies and restaurants.

Generation – Each generation or cohort is profoundly influenced by the times in which it grows up—the music, movies, politics, and defining events of that period. Members share the same major cultural, political, and economic experiences and have similar outlooks and values. Marketers often advertise to a cohort by using the icons and images prominent in its experiences. They also try to develop products and services that uniquely meet the particular interests or needs of a generational target.

Race and Culture – Multicultural marketing is an approach recognizing that different ethnic and cultural segments have sufficiently different needs and wants to require targeted marketing activities, and that a mass market approach is not refined enough for the diversity of the marketplace. The norms, language nuances, buying habits, and business practices of multicultural markets need to be factored into the initial formulation of a marketing strategy, rather than added as an afterthought. All this diversity also has implications for marketing research; it takes careful sampling to adequately profile target markets. Multicultural marketing can result in different marketing messages, media, channels, and so on. Specialized media exists to reach virtually any cultural segment or minority group, though some companies have struggled to provide financial and management support for fully realized programs.

Psychographic Segmentation

Psychographics is the science of using psychology and demographics to better understand consumers. In psychographic segmentation, buyers are divided into different groups on the basis of psychological/personality traits, lifestyle, or values. People within the same demographic group can exhibit very different psychographic profiles.

One of the most popular commercially available classification systems based on psychographic measurements is Strategic Business Insight's (SBI) VALS™ framework. VALS, signifying values and lifestyles, classifies adults into eight primary groups based on responses to a questionnaire featuring 4 demographic and 35 attitudinal questions (see Figure 6.1).

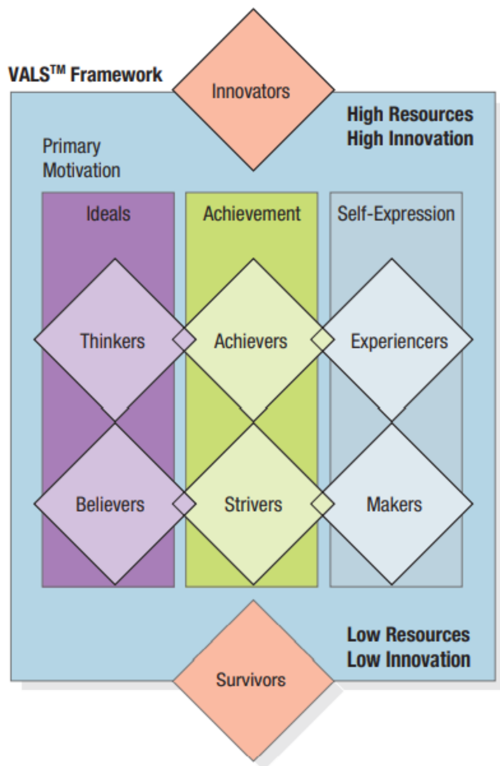

Figure 6.1: The VALS Segmentation System: An Eight-Part Typology

The main dimensions of the VALS segmentation framework are consumer motivation (the horizontal dimension) and consumer resources (the vertical dimension). Consumers are inspired by one of three primary motivations: ideals, achievement, and self-expression. Those primarily motivated by ideals are guided by knowledge and principles. Those motivated by achievement look for products and services that demonstrate success to their peers. Consumers whose motivation is self-expression desire social or physical activity, variety, and risk. Personality traits such as energy, self-confidence, intellectualism, novelty seeking, innovativeness, impulsiveness, leadership, and vanity—in conjunction with key demographics—determine an individual's resources. Different levels of resources enhance or constrain a person's expression of his or her primary motivation.

The four groups with higher resources are:

1. Innovators—Successful, sophisticated, active, "take-charge" people with high self-esteem. Purchases often reflect cultivated tastes for relatively upscale, niche-oriented products and services.
2. Thinkers—Mature, satisfied, and reflective people motivated by ideals and who value order, knowledge, and responsibility. They seek durability, functionality, and value in products.
3. Achievers—Successful, goal-oriented people who focus on career and family. They favor premium products that demonstrate success to their peers.
4. Experiencers—Young, enthusiastic, impulsive people who seek variety and excitement. They spend a comparatively high proportion of income on fashion, entertainment, and socializing.

The four groups with lower resources are:

1. Believers—Conservative, conventional, and traditional people with concrete beliefs. They prefer familiar, U.S.-made products and are loyal to established brands.
2. Strivers—Trendy and fun-loving people who are resource-constrained. They favor stylish products that emulate the purchases of those with greater material wealth.
3. Makers—Practical, down-to-earth, self-sufficient people who like to work with their hands. They seek U.S.-made products with a practical or functional purpose.
4. Survivors—Elderly, passive people concerned about change and loyal to their favorite brands.

<u>Behavioral Segmentation</u>

In behavioral segmentation, marketers divide buyers into groups on the basis of their knowledge of, attitude toward, use of, or response to a product.

Benefits sought – Consumers are divided based on the motivation they derive from their purchases. It is related to the perceived benefits they seek from product use.

Decision roles – people can be divided based on the five roles they play in a buying decision:

- Initiator, e.g. teachers or managers
- Influencer, e.g. friends or classmates
- Decider, e.g. parents or guardian
- Buyer, e.g. father or mother
- User, e.g. students

Occasions – Consumer purchases can occasionally be defined in terms of:

- The time of day, week, month, or year, or;
- Other well-defined temporal aspects of a consumer's life

User status – people can be segmented into: non-users, ex-users, potential users, first time users, and regular users of a product.

Usage Rate – Consumers can be segment into light, medium, and heavy product users. Heavy users are often a small slice but account for a high percentage of total consumption.

Buyer-Readiness Stage – Some people are unaware of the product, some are aware, some are informed, some are interested, some desire the product, and some intend to buy. To help characterize how many people are at different stages and how well they have converted people from one stage to another, marketers can employ a marketing funnel to break down the market into different buyer-readiness stages.

Loyalty Status Marketers usually envision four groups based on brand loyalty status:
- Hard-core loyals—Consumers who buy only one brand all the time
- Split loyals—Consumers who are loyal to two or three brands
- Shifting loyals—Consumers who shift loyalty from one brand to another
- Switchers—Consumers who show no loyalty to any brand

Attitude – Five consumer attitudes about products are enthusiastic, positive, indifferent, negative, and hostile.

6.2: MARKET TARGETING

Effective Segmentation Criteria

To be useful, market segments must rate favorably on five key criteria:

- **Measurable.** The size, purchasing power, and characteristics of the segments can be measured.
- **Substantial.** The segments are large and profitable enough to serve. A segment should be the largest possible homogeneous group worth going after with a tailored marketing program. It would not pay, for example, for an automobile manufacturer to develop cars for people who are less than four feet tall.
- **Accessible.** The segments can be effectively reached and served.
- **Differentiable.** The segments are conceptually distinguishable and respond differently to different marketing-mix elements and programs. If married and unmarried women respond similarly to a sale on perfume, they do not constitute separate segments.
- **Actionable.** Effective programs can be formulated for attracting and serving the segments.

POINTS TO PONDER

1. Target marketing includes three activities: market segmentation, market targeting, and market positioning. Market segments are large, identifiable groups within a market.
2. Two bases for segmenting consumer markets are consumer characteristics and consumer responses. The major segmentation variables for consumer markets are geographic, demographic, psychographic, and behavioral. Marketers use them singly or in combination.
3. To be useful, market segments must be measurable, substantial, accessible, differentiable, and actionable.

SELF CHECK

1. Many consumers and consumer advocates are critical of individualized segmentation approaches due to personal privacy concerns. They argue that technology has made it far too easy to track buyer behavior and personal information. Marketers counter that individualized segmentation can lead to privacy abuses, but that the benefits to both consumers and marketers far outweigh the risks. Where do you stand on this issue? What are the benefits and risks associated with individualized segmentation?
2. The size of the consuming population over the age of 50 continues to grow. What are some of the current ethical issues involved in targeting this age group? As this group gets older, will these issues become more or less important? Explain.
3. As the Marketing Manager, you need to look into building a segmentation strategy for your new Café Outlet. Give examples of effective criteria you would want to fulfil.

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TOPIC 7: SETTING PRODUCT STRATEGY

LEARING OUTCOMES

After studying this chapter, you should be able to:

1. Describe the characteristics and classifications of products
2. Explain the differentiation of products
3. Enumerate the strategies in building and managing product mix and product lines

INTRODUCTION

Product is the first of the four marketing mix elements (4Ps), which is the most important element. A product exists as a result of efforts by seller to match their resources with the requirements of the market. Product is seen as the central element of any company and all marketing activity is seen to centre on it. As the first of 4Ps, product is starting point of the majority of planning activities. It is something that can be adapted, differentiated, introduced, modified, or eliminated for profit-making purposes. Without a well-developed product strategy, a marketing organization will not have a long-term success. Product decisions are needed to determine the core strategy for the marketing plan.

7.1: PRODUCT STRATEGY

A product is anything that can be offered to a market for attention, acquisition, use, or consumption that might satisfy a need or want. Product can include goods, services, people, places & ideas.

Services are a form of product that consists of activities, benefits, or satisfactions offered for sale that are essentially intangible, and do not result in the ownership of anything. A company's market offering often includes tangible and intangible products. Both product & services in the end, aim to provide customer satisfaction based on needs, wants, or demands:

- **Need** – basic requirements (food, shelter, transportation)
- **Want** – specific requirement for products or services to match a need such as low-fat food, organic vegetables, luxury houses, etc.
- **Demand** – is a set of wants, plus the desire and ability to pay for the exchange.

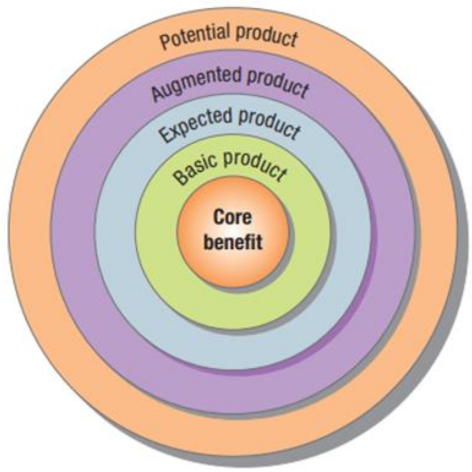

Figure 7.1: Five product level

Referring to Figure 7.1:

1. The fundamental level is the **core benefit:** the service or benefit the customer is really buying. A hotel guest is buying rest and sleep. The purchaser of a drill is buying holes. Marketers must see themselves as benefit providers.
2. At the second level, the marketer must turn the core benefit into a **basic product**. Thus, a hotel room includes a bed, bathroom, towels, desk, dresser, and closet.
3. At the third level, the marketer prepares an **expected product**, a set of attributes and conditions buyers normally expect when they purchase this product. Hotel guests minimally expect a clean bed, fresh towels, working lamps, and a relative degree of quiet.
4. At the fourth level, the marketer prepares an **augmented product** that exceeds customer expectations. In developed countries, brand positioning and competition take place at this level. In developing and emerging markets such as India and Brazil, however, competition takes place mostly at the expected product level.
5. At the fifth level stands the **potential product**, which encompasses all the possible augmentations and transformations the product or offering might undergo in the future. Here is where companies search for new ways to satisfy customers and distinguish their offering.

<u>**Product Classifications**</u>

Durability and Tangibility – Products fall into three groups according to durability and tangibility:

1. Nondurable goods are tangible goods normally consumed in one or a few uses, such as beer and shampoo. Because these goods are purchased frequently, the appropriate strategy is to make them available in many locations, charge only a small markup, and advertise heavily to induce trial and build preference.
2. Durable goods are tangible goods that normally survive many uses: refrigerators, machine tools, and clothing. Durable products normally require more personal selling and service, command a higher margin, and require more seller guarantees.
3. Services are intangible, inseparable, variable, and perishable products that normally require more quality control, supplier credibility, and adaptability. Examples include haircuts, legal advice, and appliance repairs.

Consumer-Goods Classification – When we classify the vast array of consumer goods on the basis of shopping habits, we distinguish among convenience, shopping, specialty, and unsought goods.

1. The consumer usually purchases **convenience goods** frequently, immediately, and with minimal effort. Examples include soft drinks, soaps, and newspapers. Staples are convenience goods consumers purchase on a regular basis. A buyer might routinely purchase Heinz ketchup, Crest toothpaste, and Ritz crackers. Impulse goods are purchased without any planning or search effort, like candy bars and magazines. Emergency goods are purchased when a need is urgent—umbrellas during a rainstorm, boots and shovels during the first winter snow. Manufacturers of impulse and emergency goods will place them where consumers are likely to experience an urge or compelling need to purchase.
2. **Shopping goods** are those the consumer characteristically compares on such bases as suitability, quality, price, and style. Examples include furniture, clothing, and major appliances. Homogeneous shopping goods are similar in quality but different enough in price to justify shopping comparisons. Heterogeneous shopping goods differ in product features and services that may be more important than price. The seller of heterogeneous shopping goods carries a wide assortment to satisfy individual tastes and trains salespeople to inform and advise customers.
3. **Specialty goods** have unique characteristics or brand identification for which enough buyers are willing to make a special purchasing effort. Examples include cars, stereo components, and men's suits. A Mercedes is a specialty good because interested buyers will travel far to buy one. Specialty goods don't require comparisons; buyers invest time only to reach dealers carrying the wanted products. Dealers don't need convenient locations, although they must let prospective buyers know where to find them.
4. **Unsought goods** are those the consumer does not know about or normally think of buying, such as smoke detectors. Classic examples of known but unsought goods are life insurance, cemetery plots, and gravestones. Unsought goods require advertising and personal-selling support.

Industrial-Goods Classification – Industrial goods is classified in terms of their relative cost and how they enter the production process: materials and parts, capital items, and supplies and business services. Materials and parts are goods that enter the manufacturer's product completely. They fall into two classes: raw materials, and manufactured materials and parts. Raw materials fall into two major groups: farm products (wheat, cotton, livestock, fruits, and vegetables) and natural products (fish, lumber, crude petroleum, iron ore).

Capital items – are long-lasting goods that facilitate developing or managing the finished product. They include two groups: installations and equipment. Installations consist of buildings (factories, offices) and heavy equipment (generators, drill presses, mainframe computers, elevators). Installations are major purchases. They are usually bought directly from the producer, whose sales force includes technical personnel, and a long negotiation precedes the typical sale. Producers must be willing to design to specification and to supply post-sale services. Advertising is much less important than personal selling. Equipment includes portable factory equipment and tools (hand tools, lift trucks) and office equipment (personal computers, desks). These types of equipment don't become part of a finished product. They have a shorter life than installations but a longer life than operating supplies. Although some equipment manufacturers sell direct, more often they use intermediaries, because the market is geographically dispersed, buyers are numerous, and orders are small. Quality, features, price, and service are major considerations. The sales force tends to be more important than advertising, although advertising can be used effectively.

Supplies and business service – are short-term goods and services that facilitate developing or managing the finished product. Supplies are of two kinds: maintenance and repair items (paint, nails, brooms) and operating supplies (lubricants, coal, writing paper, pencils). Together, they go under the name of MRO goods. Supplies are the equivalent of convenience goods; they are usually purchased with minimum effort on a straight-rebuy basis. They are normally marketed through intermediaries because of their low unit value and the great number and geographic dispersion of customers. Price and service are important considerations, because suppliers are standardized and brand preference is not high.

7.2: PRODUCT AND SERVICES DIFFERENTIATION

Product Differentiation

1. **Form:** Many products can be differentiated in form—the size, shape, or physical structure of a product. Consider the many possible forms of aspirin. Although essentially a commodity, it can be differentiated by dosage size, shape, color, coating, or action time.
2. **Features**: Most products can be offered with varying features that supplement their basic function. A company can identify and select appropriate new features by surveying recent buyers and then calculating customer value versus company cost for each potential feature. Marketers should consider how many people want each feature, how long it would take to introduce it, and whether competitors could easily copy it
3. **Customization:** Marketers can differentiate products by customizing them. As companies have grown proficient at gathering information about individual customers and business partners (suppliers, distributors, retailers), and as their factories are being designed more flexibly, they have increased their ability to individualize market offerings, messages, and media. Mass customization is the ability of a company to meet each customer's requirements—to prepare on a mass basis individually designed products, services, programs, and communications.
4. **Performance Quality:** Most products occupy one of four performance levels: low, average, high, or superior. Performance quality is the level at which the product's primary characteristics operate. Quality is increasingly important for differentiation as companies adopt a value model and provide higher quality for less money. Firms should design a performance level appropriate to the target market and competition, however, not necessarily the highest level possible. They must also manage performance quality through time. Continuously improving the product can produce high returns and market share; failing to do so can have negative consequences.
5. **Conformance Quality:** Buyers expect a high conformance quality, the degree to which all produced units are identical and meet promised specifications.
6. **Durability**: Durability, a measure of the product's expected operating life under natural or stressful conditions, is a valued attribute for vehicles, kitchen appliances, and other durable goods. The extra price for durability must not be excessive, however, and the product must not be subject to rapid technological obsolescence, as personal computers, televisions, and cell phones have sometimes been.
7. **Reliability**; Buyers normally will pay a premium for more reliable products. Reliability is a measure of the probability that a product will not malfunction or fail within a specified time period.
8. **Repairability**: Repairability measures the ease of fixing a product when it malfunctions or fails. Ideal repairability would exist if users could fix the product themselves with little cost in money or time. Some products include a diagnostic feature that allows service people to correct a problem over the telephone or advise the user how to correct it. Many computer hardware and

software companies offer technical support over the phone, by fax or e-mail, or via real-time chat online.

9. **Style**: Style describes the product's look and feel to the buyer. It creates distinctiveness that is hard to copy.

Services Differentiation

The main service differentiators are ordering ease, delivery, installation, customer training, customer consulting, and maintenance and repair.

1. **Ordering Ease**: Ordering ease refers to how easy it is for the customer to place an order with the company
2. **Delivery**: Delivery refers to how well the product or service is brought to the customer. It includes speed, accuracy, and care throughout the process.
3. **Installation:** Installation refers to the work done to make a product operational in its planned location. Ease of installation is a true selling point for buyers of complex products like heavy equipment and for technology novices
4. **Customer Training:** Customer training helps the customer's employees use the vendor's equipment properly and efficiently.
5. **Customer Consulting**: Customer consulting includes data, information systems, and advice services the seller offers to buyers
6. **Maintenance and Repair**: Maintenance and repair programs help customers keep purchased products in good working order
7. **Returns:** A nuisance to customers, manufacturers, retailers, and distributors alike, product returns are also an unavoidable reality of doing business, especially with online purchases. Product can be returns in two ways:
   - Controllable returns result from problems or errors by the seller or customer and can mostly be eliminated with improved handling or storage, better packaging, and improved transportation and forward logistics by the seller or its supply chain partners.
   - Uncontrollable returns result from the need for customers to actually see, try, or experience products in person to determine suitability and can't be eliminated by the company in the short run through any of these means.

7.3: PRODUCT AND BRAND RELATIONSHIP

The Product Hierarchy

The product hierarchy stretches from basic needs to particular items that satisfy those needs. We can identify six levels of the product hierarchy, using life insurance as an example:

1. **Need family**—The core need that underlies the existence of a product family. Example: security.
2. **Product family**—All the product classes that can satisfy a core need with reasonable effectiveness. Example: savings and income.
3. **Product class**—A group of products within the product family recognized as having a certain functional coherence, also known as a product category. Example: financial instruments.
4. **Product line**—A group of products within a product class that are closely related because they perform a similar function, are sold to the same customer groups, are marketed through the same outlets or channels, or fall within given price ranges. A product line may consist of

different brands, or a single-family brand, or individual brand that has been line extended. Example: life insurance.

5. **Product type**—A group of items within a product line that share one of several possible forms of the product. Example: term life insurance.
6. **Item** (also called stock-keeping unit or product variant)—A distinct unit within a brand or product line distinguishable by size, price, appearance, or some other attribute. Example: Prudential renewable term life insurance.

Product Systems and Mixes

A product system is a group of diverse but related items that function in a compatible manner. For example, the extensive iPod product system includes headphones and headsets, cables and docks, armbands, cases, power and car accessories, and speakers. A product mix (also called a product assortment) is the set of all products and items a particular seller offers for sale.

A company's product mix has a certain width, length, depth, and consistency. These concepts are illustrated in Table 7.1 for selected Procter & Gamble consumer products.

	Product Mix Width				
	Detergents	**Toothpaste**	**Bar Soap**	**Disposable Diapers**	**Paper Products**
Product Line Length	Ivory Snow (1930)	Gleem (1952)	Ivory (1879)	Pampers (1961)	Charmin (1928)
	Dreft (1933)	Crest (1955)	Camay (1926)	Luvs (1976)	Puffs (1960)
	Tide (1946)		Zest (1952)		Bounty (1965)
	Cheer (1950)		Safeguard (1963)		
	Dash (1954)		Oil of Olay (1993)		
	Bold (1965)				
	Gain (1966)				
	Era (1972)				

Table 7.1: Product Mix Width and Product Line Length for Procter & Gamble Products (including dates of introduction)

- The **width** of a product mix refers to how many different product lines the company carries. Table 7.1 shows a product mix width of five lines. (In fact, P&G produces many additional lines.)
- The length of a product mix refers to the total number of items in the mix. In Table 7.1, it is 20. We can also talk about the average **length** of a line. We obtain this by dividing the total length (here 20) by the number of lines (here 5), for an average product line length of 4.
- The **depth** of a product mix refers to how many variants are offered of each product in the line. If Tide came in two scents (Mountain Spring and Regular), two formulations (liquid and powder), and two additives (with or without bleach), it would have a depth of eight because there are eight distinct variants. We can calculate the average depth of P&G's product mix by averaging the number of variants within the brand groups.
- The **consistency** of the product mix describes how closely related the various product lines are in end use, production requirements, distribution channels, or some other way. P&G's product lines are consistent in that they are consumer goods that go through the same distribution channels. The lines are less consistent in the functions they perform for buyers.

These four product mix dimensions permit the company to expand its business in four ways. It can add new product lines, thus widening its product mix. It can lengthen each product line. It can add more product variants to each product and deepen its product mix. Finally, a company can pursue more product line consistency. To make these product and brand decisions, it is useful to conduct product line analysis.

<u>**Product Line Analysis**</u>

In offering a product line, companies normally develop a basic platform and modules that can be added to meet different customer requirements and lower production costs. Car manufacturers build cars around a basic platform. Homebuilders show a model home to which buyers can add additional features. Product line managers need to know the sales and profits of each item in their line to determine which items to build, maintain, harvest, or divest. They also need to understand each product line's market profile.

Sales and Profits – Every company's product portfolio contains products with different margins. Supermarkets make almost no margin on bread and milk, reasonable margins on canned and frozen foods, and better margins on flowers, ethnic food lines, and freshly baked goods. A telecommunication company makes different margins on its core telephone service than on added services such as call waiting, caller ID, and voice mail. Companies should recognize that items can differ in their potential for being priced higher or advertised more as ways to increase their sales, their margins, or both.

Market Profile – The product line manager must review how the line is positioned against competitors' lines. Consider paper company X with a paperboard product line. Two paperboard attributes are weight and finish quality. Paper is usually offered at standard levels of 90, 120, 150, and 180 weights. Finish quality is offered at low, medium, and high levels. Figure 7.2 shows the location of the various product line items of company X and four competitors, A, B, C, and D. Competitor A sells two product items in the extra-high weight class ranging from medium to low finish quality. Competitor B sells four items that vary in weight and finish quality. Competitor C sells three items in which the greater the weight, the greater the finish quality. Competitor D sells three items, all lightweight but varying in finish quality. Company X offers three items that vary in weight and finish quality.

The **product map** shows which competitors' items are competing against company X's items. For example, company X's low-weight, medium-quality paper competes against competitor D's and B's papers, but its high-weight, medium-quality paper has no direct competitor. The map also reveals possible locations for new items. No manufacturer offers a high-weight, low-quality paper. If company X estimates a strong unmet demand and can produce and price this paper at low cost, it could consider adding this item to its line.

Another benefit of product mapping is that it identifies market segments. Figure 7.2 shows the types of paper, by weight and quality, preferred by the general printing industry, the point-of purchase display industry, and the office supply industry. The map shows that company X is well positioned to serve the needs of the general printing industry but less effective in serving the other two industries.
Product line analysis provides information for two key decision areas—product line length and product mix pricing.

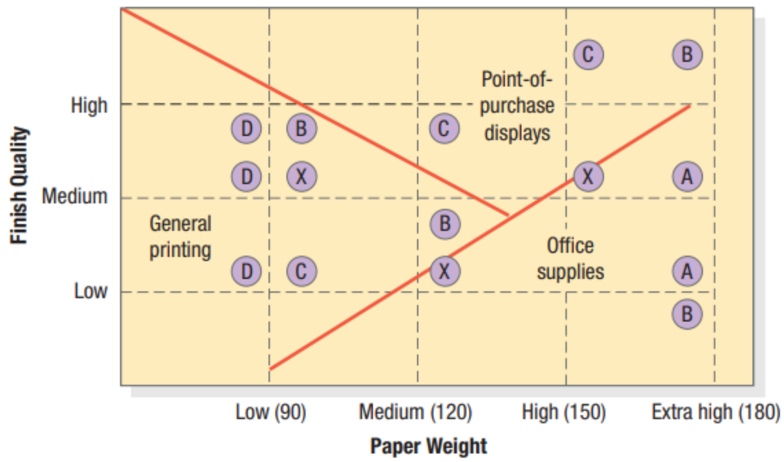

Figure 7.2: Product Map for a Paper-Product Line

Product Line Length

Company objectives influence product line length. One objective is to create a product line to induce up-selling: Thus, BMW would like to move customers up from a 3-series vehicle to a 5-series and eventually even a 7-series vehicle. A different objective is to create a product line that facilitates cross-selling: Hewlett-Packard sells printers as well as computers. Still another objective is to create a product line that protects against economic ups and downs: Electrolux offers white goods such as refrigerators, dishwashers, and vacuum cleaners under different brand names in the discount, middle-market, and premium segments, in part in case the economy moves up or down. Companies seeking high market share and market growth will generally carry longer product lines. Companies that emphasize high profitability will carry shorter lines consisting of carefully chosen items.

Line Stretching

Every company's product line covers a certain part of the total possible range. For example, Mercedes automobiles are located in the upper price range of the automobile market. Line stretching occurs when a company lengthens its product line beyond its current range, whether down-market, up-market, or both ways.

Down-Market Stretch: A company positioned in the middle market may want to introduce a lower-priced line for any of three reasons:

1. The company may notice strong growth opportunities as mass retailers such as Walmart, Best Buy, and others attract a growing number of shoppers who want value-priced goods.
2. The company may wish to tie up lower-end competitors who might otherwise try to move up-market. If the company has been attacked by a low-end competitor, it often decides to counterattack by entering the low end of the market.
3. The company may find that the middle market is stagnating or declining.

A company faces a number of naming choices in deciding to move a brand down-market:

1. Use the parent brand name on all its offerings. Sony has used its name on products in a variety of price tiers.
2. Introduce lower-priced offerings using a sub-brand name, such as P&G's Charmin Basics and Bounty Basics.

3. Introduce the lower-priced offerings under a different name, such as the Gap's Old Navy brand. This strategy is expensive to implement and means brand equity will have to be built from scratch, but the equity of the parent brand name is protected.

Up-Market Stretch: Companies may wish to enter the high end of the market to achieve more growth, realize higher margins, or simply position themselves as full-line manufacturers. Many markets have spawned surprising upscale segments: Starbucks in coffee, Häagen-Dazs in ice cream, and Evian in bottled water. The leading Japanese auto companies have each introduced an upscale automobile: Toyota's Lexus, Nissan's Infiniti, and Honda's Acura. They invented entirely new names, because consumers might not have given the brand "permission" to stretch upward when those lines were first introduced.

Two-Way Stretch: Companies serving the middle market might stretch their line in both directions. Robert Mondavi Winery, now owned by Constellation Brands, sells $35 bottles of wines as the first premium "New World wine," but it also sells $125 bottles of Mondavi Reserve at high-end wineries, restaurants, and vineyards and through direct order, as well as $11 bottles of Woodbridge created during the grape oversupply of the mid-1990s.

Line Filling
A firm can also lengthen its product line by adding more items within the present range. Motives for line filling include reaching for incremental profits satisfying dealers who complain about lost sales because of items missing from the line, utilizing excess capacity, trying to become the leading full-line company, and plugging holes to keep out competitors.

Product Mix Pricing

Marketers must modify their price-setting logic when the product is part of a product mix. In product mix pricing, the firm searches for a set of prices that maximizes profits on the total mix. Pricing is difficult because the various products have demand and cost interrelationships and are subject to different degrees of competition. We can distinguish six situations calling for product mix pricing: product line pricing, optional-feature pricing, captive-product pricing, two-part pricing, by-product pricing, and product-bundling pricing.

1. **Product Line Pricing:** Companies normally develop product lines rather than single products and introduce price steps. A men's clothing store might carry men's suits at three price levels: $300, $600, and $900, which customers associate with low-, average-, and high-quality. The seller's task is to establish perceived quality differences that justify the price differences.

2. **Optional-Feature Pricing:** Pricing options is a sticky problem, because companies must decide which to include in the standard price and which to offer separately. Many restaurants price their beverages high and their food low. The food revenue covers costs, and the beverages—especially liquor—produce the profit.

3. **Captive-Product Pricing**: Some products require the use of ancillary or captive products. Manufacturers of razors and cameras often price them low and set high markups on razor blades and film

4. **Two-Part Pricing:** Service firms engage in two-part pricing, consisting of a fixed fee plus a variable usage fee. Cell phone users pay a minimum monthly fee plus charges for calls that exceed their allotted minutes.

5. **By-Product Pricing:** The production of certain goods—meats, petroleum products, and other chemicals—often results in by-products that should be priced on their value. Any income earned on the by-products will make it easier for the company to charge a lower price on its main product if competition forces it to do so.

6. **Product-Bundling Pricing:** Sellers often bundle products and features. Pure bundling occurs when a firm offers its products only as a bundle. A talent agency might insist that a "hot" actor can be signed to a film only if the film company also accepts other talents the agency represented (directors, writers). This is a form of tied-in sales.

   In mixed bundling, the seller offers goods both individually and in bundles, normally charging less for the bundle than if the items were purchased separately. An auto manufacturer might offer an option package at less than the cost of buying all the options separately. A theater will price a season subscription lower than the cost of buying all the performances separately. Customers may not have planned to buy all the components, so savings on the price bundle must be enough to induce them to buy it.

POINTS TO PONDER

1. Product is the first and most important element of the marketing mix. Product strategy calls for making coordinated decisions on product mixes, product lines, brands, and packaging and labeling.
2. In planning its market offering, the marketer needs to think through the five levels of the product: the core benefit, the basic product, the expected product, the augmented product, and the potential product, which encompasses all the augmentations and transformations the product might ultimately undergo.
3. Products can be nondurable goods, durable goods, or services. In the consumer-goods category are convenience goods (staples, impulse goods, emergency goods), shopping goods (homogeneous and heterogeneous), specialty goods, and unsought goods. The industrial-goods category has three subcategories: materials and parts (raw materials and manufactured materials and parts), capital items (installations and equipment), and supplies and business services (operating supplies, maintenance and repair items, maintenance and repair services, and business advisory services).
4. Brands can be differentiated on the basis of product form, features, performance, conformance, durability, reliability, repairability, style, and design, as well as such service dimensions as ordering ease, delivery, installation, customer training, customer consulting, and maintenance and repair.
5. Design is the totality of features that affect how a product looks, feels, and functions. A well-designed product offers functional and aesthetic benefits to consumers and can be an important source of differentiation.
6. Most companies sell more than one product. A product mix can be classified according to width, length, depth, and consistency. These four dimensions are the tools for developing the

company's marketing strategy and deciding which product lines to grow, maintain, harvest, and divest. To analyze a product line and decide how many resources to invest in it, product line managers need to look at sales and profits and market profile.

SELF-CHECK

1. Consider the number of products available in the U.S. consumer market. In virtually every product category, consumers have many options to fulfill their needs. Are all of these options really necessary? Is having these many choices a good thing for consumers? Why or why not? Is it a good thing for marketers and retailers that have to support and carry all of these product choices? Why or why not?
2. Consider the notion that a truly effective brand is one that succinctly captures the product offering in a way that answers a question in the customer's mind. Now, consider these brands (or choose your own): Coca-Cola, Disney, Marlboro, American Express, and Ford. What questions do these brands answer? Why are these effective brands?
3. The great product selection can be classified on the basis of shopping habits and are broken down into four main areas. List these four main areas of consumer shopping habits and explain what elements are included within. Then further explain the concepts of product line width, length, depth, consistency with appropriate examples.

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LESSON 8: PRICING STRATEGY

LEARNING OUTCOMES

After studying this lesson, you should be able to:

1. Explain the background of pricing strategy
2. Discuss the steps involved in pricing a product
3. Explain the strategies in managing price setting

INTRODUCTION

In this lesson we will learn how to make effective pricing decision for a product. Since the price for a product brings revenue to the firm, having the right price will determine the profitability and the long-term survival of the firm. We will first look at the role of price in marketing followed by the steps for effective pricing of a product. We will also discuss strategy to be taken by a firm when pricing a new product, existing products and product lines.

8.1: DEFINITION & UNDERSTANDING PRICE

Price is defined as the sum of money that is charged when a person purchases a product or the total value that the person has to give up in exchange for the benefit that the person gets from the product. In an exchange process, price is important to a firm as part of the product offering. Price needs to be set right in order for a company to attract customers as it will influence whether the customer will make purchases or not.

- Profit = (Selling price X Units sold) – Total costs

  = Total Revenues – Total Costs

8.2: PRICE SETTING

<u>Step 1: Selecting the Pricing Objective</u>

The company first decides where it wants to position its market offering. The clearer a firm's objectives, the easier it is to set price. Five major objectives are: survival, maximum current profit, maximum market share, maximum market skimming, and product-quality leadership.

Survival: Companies pursue survival as their major objective if they are plagued with overcapacity, intense competition, or changing consumer wants. As long as prices cover variable costs and some fixed costs, the company stays in business. Survival is a short-run objective; in the long run, the firm must learn how to add value or face extinction.

Maximum Current Profit: Many companies try to set a price that will maximize current profits. They estimate the demand and costs associated with alternative prices and choose the price that produces maximum current profit, cash flow, or rate of return on investment. This strategy assumes the firm knows its demand and cost functions; in reality, these are difficult to estimate. In emphasizing current performance, the company may sacrifice long-run performance by ignoring the effects of other marketing variables, competitors' reactions, and legal restraints on price.

Maximum Market Share: Some companies want to maximize their market share. They believe a higher sales volume will lead to lower unit costs and higher long-run profit. They set the lowest price, assuming the market is price sensitive.

Maximum Market Skimming: Companies unveiling a new technology favor setting high prices to maximize market skimming. Market skimming makes sense under the following conditions: (1) A sufficient number of buyers have a high current demand; (2) the unit costs of producing a small volume are high enough to cancel the advantage of charging what the traffic will bear; (3) the high initial price does not attract more competitors to the market; (4) the high price communicates the image of a superior product.

Product-Quality Leadership: A company might aim to be the product-quality leader in the market. Many brands strive to be "affordable luxuries"—products or services characterized by high levels of perceived quality, taste, and status with a price just high enough not to be out of consumers' reach.

Other Objectives: Nonprofit and public organizations may have other pricing objectives. A university aims for partial cost recovery, knowing that it must rely on private gifts and public grants to cover its remaining costs. A nonprofit hospital may aim for full cost recovery in its pricing. A nonprofit theater company may price its productions to fill the maximum number of seats. A social service agency may set a service price geared to client income. Whatever the specific objective, businesses that use price as a strategic tool will profit more than those that simply let costs or the market determine their pricing.

Step 2: Determining Demand

Each price will lead to a different level of demand and have a different impact on a company's marketing objectives. The normally inverse relationship between price and demand is captured in a demand curve (see Figure 8.1): The higher the price, the lower the demand. For prestige goods, the demand curve sometimes slopes upward. One perfume company raised its price and sold more rather than less! Some consumers take the higher price to signify a better product. However, if the price is too high, demand may fall.

Price Sensitivity: The demand curve shows the market's probable purchase quantity at alternative prices. It sums the reactions of many individuals with different price sensitivities. The first step in estimating demand is to understand what affects price sensitivity. Generally speaking, customers are less price sensitive to low-cost items or items they buy infrequently. They are also less price sensitive when (1) there are few or no substitutes or competitors; (2) they do not readily notice the higher price; (3) they are slow to change their buying habits; (4) they think the higher prices are justified; and (5) price is only a small part of the total cost of obtaining, operating, and servicing the product over its lifetime.

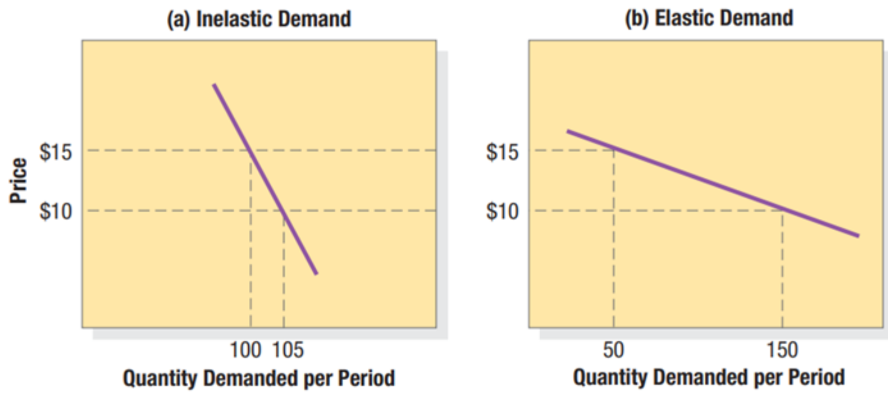

Figure 8.1: Inelastic and Elastic Demand

Estimating Demand Curves: Most companies attempt to measure their demand curves using several different methods.

1. **Surveys** can explore how many units' consumers would buy at different proposed prices. Although consumers might understate their purchase intentions at higher prices to discourage the company from pricing high, they also tend to actually exaggerate their willingness to pay for new products or services.
2. **Price** experiments can vary the prices of different products in a store or charge different prices for the same product in similar territories to see how the change affects sales
3. **Statistical analysis** of past prices, quantities sold, and other factors can reveal their relationships. The data can be longitudinal (over time) or cross-sectional (from different locations at the same time). Building the appropriate model and fitting the data with the proper statistical techniques calls for considerable skill, but sophisticated price optimization software and advances in database management have improved marketers' abilities to optimize pricing.

Price Elasticity of Demand: Marketers need to know how responsive, or elastic, demand is to a change in price. Consider the two demand curves in Figure 14.1. In demand curve (a), a price increase from $10 to $15 leads to a relatively small decline in demand from 105 to 100. In demand curve (b), the same price increase leads to a substantial drop in demand from 150 to 50. If demand hardly changes with a small change in price, we say the demand is inelastic. If demand changes considerably, demand is elastic.

The higher the elasticity, the greater the volume growth resulting from a 1 percent price reduction. If demand is elastic, sellers will consider lowering the price. A lower price will produce more total revenue. This makes sense as long as the costs of producing and selling more units do not increase disproportionately.

Price elasticity depends on the magnitude and direction of the contemplated price change. It may be negligible with a small price change and substantial with a large price change. It may differ for a price cut versus a price increase, and there may be a price indifference band within which price changes have little or no effect.

Finally, long-run price elasticity may differ from short-run elasticity. Buyers may continue to buy from a current supplier after a price increase but eventually switch suppliers. Here demand is more elastic in the long run than in the short run, or the reverse may happen: Buyers may drop a supplier after a price increase but return later. The distinction between short-run and long-run elasticity means that sellers will not know the total effect of a price change until time passes.

Step 3: Estimating Costs

Demand sets a ceiling on the price the company can charge for its product. Costs set the floor. The company wants to charge a price that covers its cost of producing, distributing, and selling the product, including a fair return for its effort and risk. Yet when companies price products to cover their full costs, profitability isn't always the net result.

Types of Costs and Levels of Production: A company's costs take two forms, fixed and variable. **Fixed costs**, also known as overhead, are costs that do not vary with production level or sales revenue. A company must pay bills each month for rent, heat, interest, salaries, and so on regardless of output.

Variable costs vary directly with the level of production. For example, each hand calculator produced by Texas Instruments incurs the cost of plastic, microprocessor chips, and packaging. These costs tend to be constant per unit produced, but they're called variable because their total varies with the number of units produced.

Total costs consist of the sum of the fixed and variable costs for any given level of production. **Average cost** is the cost per unit at that level of production; it equals total costs divided by production. Management wants to charge a price that will at least cover the total production costs at a given level of production.

Target Costing: Costs change with production scale and experience. They can also change as a result of a concentrated effort by designers, engineers, and purchasing agents to reduce them through **target costing**. Market research establishes a new product's desired functions and the price at which it will sell, given its appeal and competitors' prices. This price less desired profit margin leaves the target cost the marketer must achieve. The firm must examine each cost element—design, engineering, manufacturing, sales—and bring down costs so the final cost projections are in the target range.

Step 4: Analyzing Competitors' Costs, Prices, and Offers

Within the range of possible prices determined by market demand and company costs, the firm must take competitors' costs, prices, and possible price reactions into account. If the firm's offer contains features not offered by the nearest competitor, it should evaluate their worth to the customer and add that value to the competitor's price. If the competitor's offer contains some features not offered by the firm, the firm should subtract their value from its own price. Now the firm can decide whether it can charge more, the same, or less than the competitor.

The introduction or change of any price can provoke a response from customers, competitors, distributors, suppliers, and even government. Competitors are most likely to react when the number of firms is few, the product is homogeneous, and buyers are highly informed.

How can a firm anticipate a competitor's reactions? One way is to assume the competitor reacts in the standard way to a price being set or changed. Another is to assume the competitor treats each price difference or change as a fresh challenge and reacts according to self-interest at the time. Now the company will need to research the competitor's current financial situation, recent sales, customer loyalty, and corporate objectives. If the competitor has a market share objective, it is likely to match price differences or changes. If it has a profit-maximization objective, it may react by increasing its advertising budget or improving product quality.

The problem is complicated because the competitor can put different interpretations on lowered prices or a price cut: that the company is trying to steal the market, that it is doing poorly and trying to boost its sales, or that it wants the whole industry to reduce prices to stimulate total demand.

<u>**Step 5: Selecting a Pricing Method**</u>

Given the customers' demand schedule, the cost function, and competitors' prices, the company is now ready to select a price. We will examine six price-setting methods: markup pricing, target-return pricing, perceived-value pricing, value pricing, going-rate pricing, and auction-type pricing.

1. **Markup Pricing**: The most elementary pricing method is to add a standard markup to the product's cost. Construction companies submit job bids by estimating the total project cost and adding a standard markup for profit. Lawyers and accountants typically price by adding a standard markup on their time and costs.

Variable cost per unit	\$10
Fixed costs	\$300,000
Expected unit sales	50,000

Suppose a toaster manufacturer has the following costs and sales expectations: The manufacturer's unit cost is given by:

$$\text{Unit cost} = \text{variable cost} + \frac{\text{fixed cost}}{\text{unit sales}} = \$10 + \frac{\$300{,}00}{50{,}000} = \$16$$

Now assume the manufacturer wants to earn a 20 percent markup on sales. The manufacturer's markup price is given by:

$$\text{Markup price} = \frac{\text{unit cost}}{(1 - \text{desired return on sales})} = \frac{\$16}{1 - 0.2} = \$20$$

The manufacturer will charge dealers \$20 per toaster and make a profit of \$4 per unit. If dealers want to earn 50 percent on their selling price, they will mark up the toaster 100 percent to \$40. Markups are generally higher on seasonal items (to cover the risk of not selling), specialty items, slower-moving items, items with high storage and handling costs, and demand-inelastic items, such as prescription drugs. Does the use of standard markups make logical sense? Generally, no. Any pricing method that ignores current demand, perceived value, and competition is not likely to lead to the optimal price. Markup pricing works only if the marked-up price actually brings in the expected level of sales.

Still, markup pricing remains popular. First, sellers can determine costs much more easily than they can estimate demand. By tying the price to cost, sellers simplify the pricing task. Second, where all firms in the industry use this pricing method, prices tend to be similar and price competition is minimized. Third, many people feel that cost-plus pricing is fairer to both buyers and sellers. Sellers do not take advantage of buyers when the latter's demand becomes acute, and sellers earn a fair return on investment.

2. **Target-Return Pricing**: In target-return pricing, the firm determines the price that yields its target rate of return on investment. Public utilities, which need to make a fair return on investment, often use this method. Suppose the toaster manufacturer has invested $1 million in the business and wants to set a price to earn a 20 percent ROI, specifically $200,000. The target-return price is given by the following formula:

$$\text{Target-return price} = \text{unit cost} + \frac{\text{desired return} \times \text{invested capital}}{\text{unit sales}}$$

$$= \$16 + \frac{.20 \times \$1{,}000{,}000}{50{,}000} = \$20$$

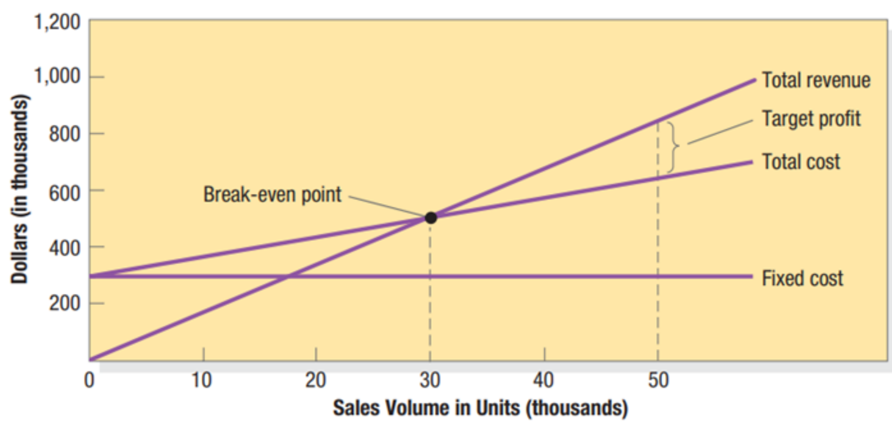

Figure 8.2: Break-Even Chart for Determining Target-Return Price and Break-Even Volume

The manufacturer will realize this 20 percent ROI provided its costs and estimated sales turn out to be accurate. But what if sales don't reach 50,000 units? The manufacturer can prepare a break-even chart to learn what would happen at other sales levels (see Figure 8.2). Fixed costs are $300,000 regardless of sales volume. Variable costs, not shown in the figure, rise with volume. Total costs equal the sum of fixed and variable costs.

The total revenue curve starts at zero and rises with each unit sold. The total revenue and total cost curves cross at 30,000 units. This is the break-even volume. We can verify it by the following formula:

$$\text{Break-even volume} = \frac{\text{fixed cost}}{(\text{price} - \text{variable cost})} = \frac{\$300{,}000}{\$20 - \$10} = 30{,}000$$

The manufacturer, of course, is hoping the market will buy 50,000 units at $20, in which case it earns $200,000 on its $1 million investment, but much depends on price elasticity and competitors' prices. Unfortunately, target-return pricing tends to ignore these considerations.

The manufacturer needs to consider different prices and estimate their probable impacts on sales volume and profits. The manufacturer should also search for ways to lower its fixed or variable costs, because lower costs will decrease its required break-even volume.

3. **Perceived-Value Pricing:** An increasing number of companies now base their price on the customer's perceived value. Perceived value is made up of a host of inputs, such as the buyer's image of the product performance, the channel deliverables, the warranty quality, customer support, and softer attributes such as the supplier's reputation, trustworthiness, and esteem. Companies must deliver the value promised by their value proposition, and the customer must perceive this value. Firms use the other marketing program elements, such as advertising, sales force, and the Internet, to communicate and enhance perceived value in buyers' minds.

4. **Value Pricing:** In recent years, several companies have adopted value pricing: They win loyal customers by charging a fairly low price for a high-quality offering. Value pricing is thus not a matter of simply setting lower prices; it is a matter of reengineering the company's operations to become a low-cost producer without sacrificing quality, to attract a large number of value-conscious customers. Value pricing can change the manner by which a company sets prices too. One company that sold and maintained switch boxes in a variety of sizes for telephone lines found that the probability of failure—and thus maintenance costs—was proportional to the number of switches customers had in their boxes rather than to the dollar value of the installed boxes. The number of switches could vary in a box, though. Therefore, rather than charging customers based on the total spent on their installation, the company began charging based on the total number of switches needing servicing.

5. **Going-Rate Pricing:** In going-rate pricing, the firm bases its price largely on competitors' prices. In oligopolistic industries that sell a commodity such as steel, paper, or fertilizer, all firms normally charge the same price. Smaller firms "follow the leader," changing their prices when the market leader's prices change rather than when their own demand or costs change. Some may charge a small premium or discount, but they preserve the difference. Thus, minor gasoline retailers usually charge a few cents less per gallon than the major oil companies, without letting the difference increase or decrease. Going-rate pricing is quite popular. Where costs are difficult to measure or competitive response is uncertain, firms feel the going price is a good solution because it is thought to reflect the industry's collective wisdom.

6. **Auction-Type Pricing:** Auction-type pricing is growing more popular, especially with scores of electronic marketplaces selling everything from pigs to used cars as firms dispose of excess inventories or used goods. pulls are the bid's expected profit. To buy equipment for its drug researchers, Pfizer uses reverse auctions in which suppliers submit online the lowest price they are willing to be paid. If the increased savings a firm obtains in an online auction translates into decreased margins for an incumbent supplier, however, the supplier may feel the firm is opportunistically squeezing out price concessions. Online auctions with a large number of bidders, greater economic stakes, and less visibility in pricing result in greater overall satisfaction, more positive future expectations, and fewer perceptions of opportunism.

Step 6: Selecting the Final Price

Pricing methods narrow the range from which the company must select its final price. In selecting that price, the company must consider additional factors, including the impact of other marketing activities, company pricing policies, gain-and-risk-sharing pricing, and the impact of price on other parties.

Impact of Other Marketing Activities

The final price must consider the brand's quality and advertising relative to the competition. In a classic study, Paul Farris and David Reibstein examined the relationships among relative price, relative quality, and relative advertising for 227 consumer businesses and found the following:

- Brands with average relative quality but high relative advertising budgets could charge premium prices. Consumers were willing to pay higher prices for known rather than for unknown products.
- Brands with high relative quality and high relative advertising obtained the highest prices. Conversely, brands with low quality and low advertising charged the lowest prices.
- For market leaders, the positive relationship between high prices and high advertising held most strongly in the later stages of the product life cycle.

These findings suggest that price is not necessarily as important as quality and other benefits.

Company Pricing Policies

The price must be consistent with company pricing policies. Yet companies are not averse to establishing pricing penalties under certain circumstances. Many companies set up a pricing department to develop policies and establish or approve decisions. The aim is to ensure that salespeople quote prices that are reasonable to customers and profitable to the company.

Gain-And-Risk-Sharing Pricing

Buyers may resist accepting a seller's proposal because of a high perceived level of risk. The seller has the option of offering to absorb part or all the risk if it does not deliver the full promised value. Some recent risk-sharing applications include big computer hardware purchases and health plans for big unions.

Impact of Price on Other Parties

How will distributors and dealers feel about the contemplated price? If they don't make enough profit, they may choose not to bring the product to market. Will the sales force be willing to sell at that price? How will competitors react? Will suppliers raise their prices when they see the company's price? Will the government intervene and prevent this price from being charged?

POINTS TO PONDER

1. Despite the increased role of nonprice factors in modern marketing, price remains a critical element of marketing. Price is the only element that produces revenue; the others produce costs. Pricing decisions have become more challenging, however, in a changing economic and technological environment.
2. In setting pricing policy, a company follows a six-step procedure. It selects its pricing objective. It estimates the demand curve, the probable quantities it will sell at each possible price. It estimates how its costs vary at different levels of output, at different levels of accumulated production experience, and for differentiated marketing offers. It examines competitors' costs, prices, and offers. It selects a pricing method, and it selects the final price.

SELF-CHECK

1. One of the key themes of today's economy is the challenge of marketing goods and services in mature markets that are plagued by commoditization. In what ways is pricing strategy related to commoditization? How can a firm offer good value in a mature market where price is the only visible means of differentiation? Are most firms too concerned about their costs to really deliver value in other ways? Explain.
2. Pricing strategy associated with services is typically more complex than the pricing of tangible goods. As a consumer, what pricing issues do you consider when purchasing services? How difficult is it to compare prices among competing services, or to determine the complete price of the service before purchase? What could service providers do to solve these issues?
3. Price elasticity often varies for the same product based on the situation. What situational factors might affect the price elasticity of these products:
    a. sporting event or concert tickets?
    b. staple goods such as milk, eggs, or bread?
    c. an electric razor?
    d. eye surgery to correct vision?

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LESSON 9: DISTRIBUTION CHANNEL STRATEGY

LEARNING OUTCOMES

After studying this lesson, you should be able to:

1. Explain the supply chain management and value delivery network
2. Discuss the function and activities of marketing channel members
3. Discuss the choice of channel design for different markets
4. Explain the meaning and functions of marketing logistics

INTRODUCTION

The distribution channel, or place strategy will focus on how products are made available to target customers through marketing channels and marketing logistics. Decisions on distribution of a product are not exclusive from other marketing mix strategies, and will depend on the types of product. The decisions will also determine the price structure of the product and how it will be promoted. In order to understand place or distribution decisions, we will first look at the supply chain and value delivery network, the nature of marketing channels and their various functions, and the different types of channel institutions.

9.1: SUPPLY CHAIN AND VALUE DELIVERY NETWORK

Supply Chain: Place or distribution decision is an activity that is a part of the higher supply chain management. Supply chain refers to the entire spectrum of activities involved- from the supply of raw materials and resources for production, to the production of the products, and to the distribution of products to end users. In an industry, the whole process of the supply resources for the production of the products is known as the upstream activities of the supply chain management. On the other hand, the process that involves the distribution of finished goods to the manufacturers' resellers and the delivery of products to the end users is known as the downstream activities.

Value delivery network: A larger perspective of supply chain management is the value delivery network. Besides addressing the physical supply, value delivery network includes the partnership of the various parties involved in ensuring the supply chain activities are managed effectively & efficiently.

9.2: THE NATURE OF MARKETING CHANNELS

A **marketing channel** is a set of downstream processes of a supply chain that focuses on the flow of ownership of products from the manufacturer to the end users. Manufacturers use channels of distribution in order to deliver finished goods or services to customers.

Figure 9.1: Intermediaries in the Marketing Channel

Based on Figure 9.1, please refer to Table 9.1.

Type of Intermediary	Function	Product Ownership	Income Generation
Wholesalers	Distribute products to other intermediaries	Buy, take title and physical possession of products	Earn profit
Retailers	Distribute products to end users	Buy, take title and physical possession of products	Earn profit
Brokers	Bring buyers and sellers together for a transaction	Do not take title of products	Earn commission
Agents	Represent either buyers or sellers on a permanent basis	Do not take title of products	Earn commission

Table 9.1: Intermediaries – their functions and income generation

<u>**The role of Intermediaries in a Marketing Channel**</u>

Figure 9.2: The role of Intermediaries

1. **Overcoming discrepancy:**
    a. Quantity discrepancy – refers to the differences between the economical amount of production by manufactures and the amount of end users want to buy.
    b. Assortment discrepancy – means a lack of items needed to receive full satisfaction from a product.
    c. Temporal discrepancy – is created when a product is produced, but the consumers are not ready to purchase it at the time of production.

   d. Spatial discrepancy – exists from the difference between the location of the producer and the location of widely scattered markets.
2. **Providing specialization:**
   a. Information – intermediaries in their day-to-day dealings gather and distribute details about the market and the environment.
   b. Promotion – Intermediaries communicate product benefits to customers through marketing communications materials
   c. Negotiation – Intermediaries discuss on price and other terms in distribution channel transaction.
   d. Physical distribution – intermediaries move and store goods physically.
   e. Financing – intermediaries fund the transactions in the distribution channel by giving credits or allowing credit card purchase.
3. **Contact efficacy** – marketing channels reduce the number of transactions needed to pass products from manufacturers to consumers. Retailers assemble a selection of merchandise so that a buying trip (one contact) can result in many different items. Channel members also allow producers and buyers to reduce the number of transactions each must make.

   Consider this situation: If five consumers wish to buy products from three different manufacturers, there will be a total of fifteen transactions. But, with intermediaries, the number of transactions will be five. What is there is no retailers? How many contacts with manufacturers would you have to make in order to buy your monthly sustenance? You would be probably exhausted by the time you purchase a box of toothpaste from Colgate – Palmolive, a bottle of Nescafe from Nestle, and a bottle of cooking oil from Lam Soon.

9.3: MARKETING CHANNEL STRUCTURES

Marketing Channel Structures

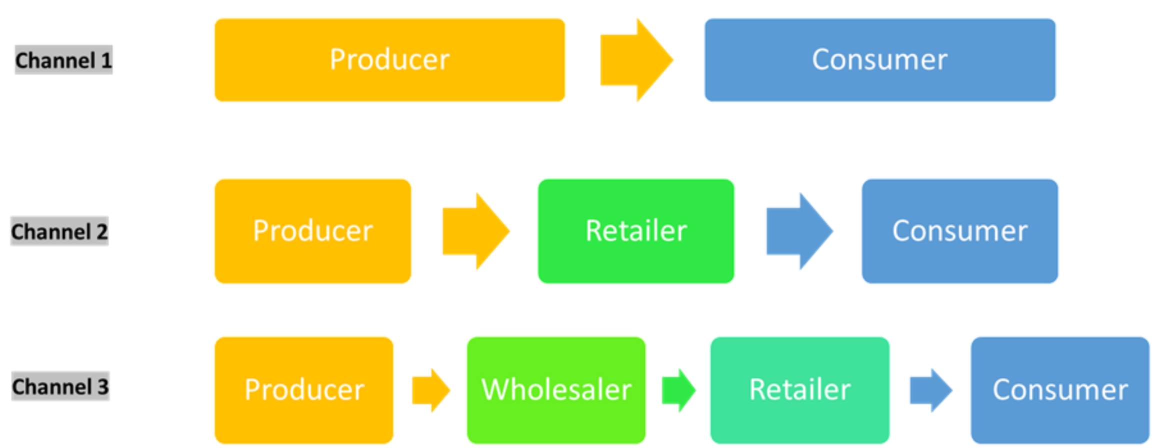

Figure 9.3: Marketing Channels for the Consumer Market

Based on Figure 9.3; Channel 1 is the direct channel while both Channel 2 and 3 are indirect channels. Channel 2 is known as retailer channel while Channel 3 is known as a wholesaler channel. The number of intermediaries in the channel determines the channel length.

Direct Channel – The simplest consumer product channel involves the direct channel to sell directly to consumers. Producers do not use intermediaries to deliver the products to the consumers.

Indirect Channel – Include one or more intermediaries in the route. Retailer channels: includes retailers that stand between the producers and the customers. Wholesaler channel: has both wholesalers and retailers in the channel. The goods move from the produces to the wholesalers to the retailers, and finally to the consumers.

A short channel vs Long channel

1. A **short channel** has fewer levels of intermediaries. It is more suitable for:
   - Service which require personal interaction between providers and users
   - Business markets due to its large volume purchases, and business are concentrated geographically
   - Perishables
   - Products that require high technical knowledge to operate
   - Products that are bulky
   - Manufacturers who want higher control on value delivery

2. A **long channel** has more levels of intermediaries between manufacturer & consumers. The manufacturer has lesser control on value delivery to end users, but in most cases, the intermediaries are established & trusted.
   - Convenience products that require intensive distribution
   - Channel networks which have well-experienced and established intermediaries in the market
   - High distribution costs that can be shared by more intermediaries
   - Value delivery that requires less control

9.4: MARKETING CHANNEL DESIGN DECISION

In order to design the distribution channel structure for products, marketers need to determine the customer distribution requirements, company's service output level, number of intermediaries in the network and types of intermediaries.

Number of Intermediaries

Figure 9.4: Spectrum of distribution intensity design decision

Exclusive distribution – involves a limited number of intermediaries handling the firm's products and services. It is used when the firm wants to have more control in handling the product such as on the service level and the service output.

Intensive distribution – is to place the goods or services in as many outlets as possible. It is often being used when consumers demand a great deal of convenience.

Selective distribution – involves the use of more than a few but less than all the intermediaries who are willing to carry a particular product. Selective distribution enables the producer to gain adequate market coverage with more control and less cost than intensive distribution.

Types of Intermediaries

Wholesalers: Unlike agents & brokers, wholesalers take ownership of the products. Full service merchant wholesalers perform a wide variety of tasks for the suppliers and customers. Limited service merchant wholesalers perform the buying & storage function but normally require their customers to do their own transporting and financing tasks. The functions of the wholesalers are:

- Buying & selling
- Assortment building
- Bulk-breaking
- Warehousing
- Transportation
- Financing
- Market information

Retailers – Retailing is defined as all activities performed related with selling of goods by a firm to the final users of products. Types of Store Retailers – There are many types of store retailers. They differ in the extent of:

- The product lines they carry
- The type of consumer search effort they practice

- The level of service offered

Product Assortment	Relative Price Emphasis	Level of Service Provided	Ownership
• Departmental stores • Department centres • Hypermarkets • Supermarkets • Mini markets and provision shops • Specialty stores • Category killers • Specialty centres • Convenience stores • Sundry/toiletry shops • Pharmacies • Chinese medicinal halls	• Discount stores • Off-price retailers	• Self-service • Limited service • Full service	• Corporate chain • Voluntary chain & retailer cooperative • Consumer cooperative • Franchise organization • Merchandise conglomerate

Table 9.2: Categories of Retailers

9.5: MARKETING LOGISTICS

Marketing Logistics, which is also known as physical distribution, is considered after decisions on the marketing channel have been made. Logistics involves getting the right amount of the right product to the right place and at the right time.

Figure 9.5: Main Logistics Function

POINTS TO PONDER

1. Most producers do not sell their goods directly to final users. Between producers and final users stands one or more marketing channels, a host of marketing intermediaries performing a variety of functions.
2. Marketing channel decisions are among the most critical decisions facing management. The company's chosen channel(s) profoundly affect all other marketing decisions.

3. Companies use intermediaries when they lack the financial resources to carry out direct marketing, when direct marketing is not feasible, and when they can earn more by doing so. The most important functions performed by intermediaries are information, promotion, negotiation, ordering, financing, risk taking, physical possession, payment, and title.
4. Manufacturers have many alternatives for reaching a market. They can sell direct or use one-, two-, or three-level channels. Deciding which type(s) of channel to use calls for analyzing customer needs, establishing channel objectives, and identifying and evaluating the major alternatives, including the types and numbers of intermediaries involved in the channel.

SELF-CHECK

1. Some manufacturers and retailers advertise that customers should buy from them because they "eliminate the middleman." Evaluate this comment in light of the functions that must be performed in a marketing channel. Does a channel with fewer members always deliver products to customers at lower prices? Defend your position.
2. Describe the characteristics of a product that represents something you would go to great lengths to acquire, thus supporting a manufacturer's use of an exclusive distribution strategy. Why is the service better and the salespeople more knowledgeable at an exclusive distribution location versus an intensive distribution location?
3. What are the major differences you have experienced in buying a product through a traditional retail store, a manufacturer's physical store, a catalog, and an online merchant? What have some retailers in your area done to justify their ongoing presence in the channel?

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LESSON 10: INTEGRATED MARKETING COMMUNICATIONS STRATEGY

LEARNING OUTCOMES

After studying this lesson, you should be able to:
1. Explain the role of marketing communication
2. Describe the communication mix
3. Discuss the major steps in developing effective communications
4. Enumerate the integrated marketing communications elements and tools

INTRODUCTION

Modern marketing calls for more than developing a good product, attractive price, and accessibility to target customers. Companies must also know how to communicate effectively with present and potential customers, stakeholders as well as with the general public. In the past, a number of terms have been used in the field of marketing communications, the most common of which appear to be 'advertising' and 'promotion'. These two words helps define what marketing and communications entail, namely the pushing forward of products or services and the turning if the consumer towards the product or service. Once these two elements are met there is a chance of a sale.

10.1: THE MARKETING COMMUNICATION

Marketing communication mix is the last P (promotion) of the 4Ps of marketing mix which covers every method and medium of communicating with the target audience. Marketing communications perform many functions for consumers such as:
- To tell or show how and why a product is used
- To inform who is best suited for a product
- To inform where and when a product is used
- To educate consumers about a product, company and what it stands for,
- To allow consumers to be given an incentive or reward for usage or trial, and
- To allow companies to link their brands to people, places, feelings and events.

Marketing communications program plays an important role in the building up brand equity. Creating a brand image and building brand awareness is done through the medium of marketing communication; in its most common form called advertising.

To develop effective communications, marketers need to carry out the eight steps suggested below:
1. Identify the target audience
2. Determine the communication objectives
3. Design the communication
4. Select the communication channels
5. Establish the total communication budget
6. Decide on the communication mix
7. Measure the communications' results

8. Manage the integrated marketing communication process

10.2: INTEGRATED MARKETING COMMUNICATIONS

Integrated Marketing Communications (IMC) is defined as the strategic, coordinated use of promotion to create one consistent message across multiple channels to ensure maximum persuasive impact on the firm's current and potential customers. **The Importance of IMC:**

- Foster's long-term relationships
- Reduces or eliminates promotional redundancies
- Technology allows better targeting of customers

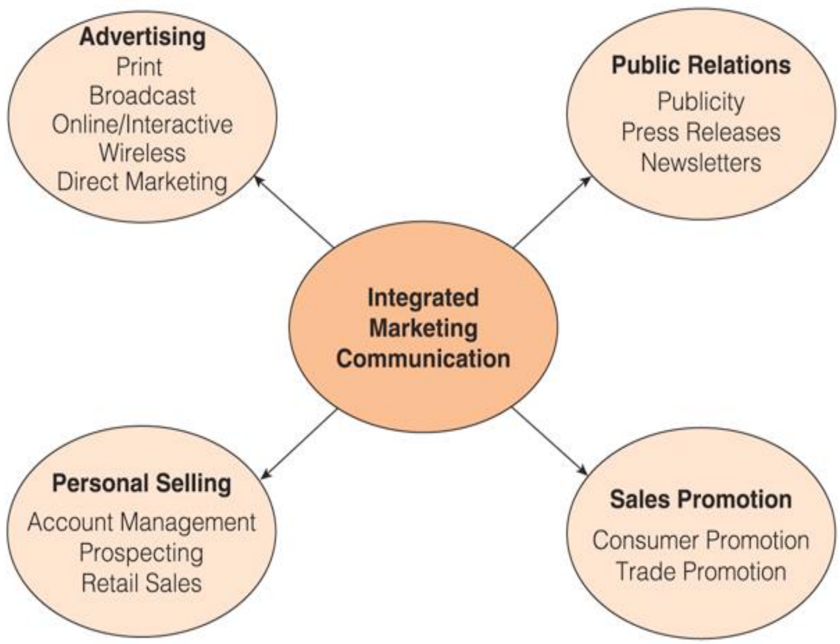

Figure 10.1: Components of IMC Strategy

<u>**Strategic Issues in Integrated Marketing Communications (IMC)**</u>

IMC must have clear promotional goals and objectives.

The AIDA Model – The acronym AIDA stands for Attention, Interest, Desire and Action. These are the four stages that a consumer goes through when watching or viewing an advertisement.

1. **Attention** – is usually grabbed by the use of image, color, layout, typography, size, celebrity, model etc.
2. **Interest** – Once attention is grabbed, it's necessary to create interest in the viewers mind so that they will read more about the brand being advertised. By the use of an attractive sub head, interest can be invoked.

3. **Desire** – The element of desire is usually created by the use of body copy where you write in detail about the necessity of buying the brand, thereby explaining the features of the brand, facts and figures.
4. **Action** – Towards the end, the contact information of the brand will be given where they expect the viewers to act immediately. It can be in the form of shop address, toll free numbers or website address

An advertisements success depends up on the viewer's ability to notice and understand its message. The AIDA model helps the copy writer to present the elements of a print ad, Headline, Subhead, Body copy, slogan and contact information in a format that makes the viewers read in a flow and understand about the product easily.

<u>**Promotional Strategy Over the Product Life Cycle**</u>

Introduction	Promotion depends on heavy advertising and public relations to build brand awareness and educate customers on the product's benefits. Personal selling ensures distribution coverage and supply chain cooperation. Consumer sales promotion stimulates product trial, while trade sales promotion facilitates or expedites distribution activities, especially in obtaining favorable shelf space or product display.
Growth	To sustain growth, firms spend heavily on advertising and public relations to build and maintain brand loyalty. Personal selling maintains distribution and supply chain cooperation. Sales promotion activities decline in importance.
Maturity	A firm's use of advertising shifts to emphasize reminding customers of the firm's products. Sales promotion efforts strongly encourage brand switching for both consumers and the trade. Personal selling remains important to ensure supply chain support and distribution coverage.
Decline	Firms begin to drastically reduce their advertising and public relations efforts in an attempt to reduce expenses. Sales promotion and personal selling drop to levels that are just sufficient enough to maintain product support.

Table 10.1: Promotional Strategy Over the Product Life Cycle

Buyer Readiness Stage

- Advertising and publicity play the most important roles in the awareness building stage
- Customer comprehension is primarily affected by advertising and personal selling.
- Customer conviction is influenced mostly by personal selling
- Closing the sale is influenced mostly by personal selling and sales promotion
- Reordering is affected mostly by personal selling, sales promotion, and somewhat by advertising.

10.3: THE MAJOR MODES OF COMMUNICATION IN MARKETING MIX

<u>**Communication Platforms**</u>

1. **Advertising:**
   - Print and broadcast ads
   - Packaging
   - Cinema

- Brochures
- Posters
- Billboards
- Display signs
- Point of purchase displays

2. **Sales Promotion**
   - Contests, games, sweepstakes, lotteries
   - Premiums and gifts
   - Sampling
   - Fairs and trade shows
   - Coupons
   - Rebates
   - Trade-in allowances
   - Tie-ins
3. **Events and Experiences**
   - Sports
   - Entertainment
   - Festivals
   - Arts
   - Causes
   - Factory tours
   - Company museums
   - Street activities
4. **Public Relations and Publicity**
   - Press kits
   - Speeches
   - Seminars
   - Annual reports
   - Charitable donations
   - Publications
   - Lobbying
   - Company magazine
5. **Direct and Interactive Marketing**
   - Catalogues
   - Mailings
   - Telemarketing
   - Electronic shopping
   - TV shopping
   - Email
   - Company blogs
   - Web sites
6. **Personal Selling**
   - Sales presentations
   - Samples
   - Incentive programs

- Fairs / trade shows

7. **Word-of-Mouth**
   - Person-to-person
   - Chat rooms/Blogs

Modes of Communication in Marketing Mix

1. **Advertising:**
   - Advertising can be used to build up a long-term image for a product or trigger quick sales.
   - It can efficiently reach geographically dispersed buyers, and it creates presumption in consumers that the advertised brand must offer a "good value".
   - Certain types of advertising require large budgets; others do not
   - The presence of advertisement itself has impact on sales
   - It is hard to make generalization on advertising.
   - Very cost efficient when used to reach a mass audience
   - Traditional mass audiences are fragmenting due to increasing media options
   - Digital communication (Internet, mobile) is the fastest growing form of advertising.
   - Traditional media (newspapers, radio, magazines) are struggling for relevance.

   Types of Advertising:
   - Institutional advertising – focused on establishing an image or identity of a company into the minds of the audience.
   - Advocacy advertising – advertisement that attempts to influence public opinion on specific political, economic & social issues
   - Product advertising – promotes the sale of products and services

   Determining the Advertising Budget:
   - Percentage of sales approach
   - Objectives and task approach
   - Competitive matching approach
   - Arbitrary approach

   Evaluating Advertising Effectiveness:
   - Key Considerations:
     - Evaluating the achievement of advertising objectives
     - Assessing the effectiveness of advertising copy, illustrations, and layouts
     - Evaluating the effectiveness of various media
   - Timing of Evaluations:
     - Pre-test
     - During
     - Post-test

2. **Public Relations**

Public relations (PR) involve a variety of programs designed to promote or protect a company's image to its individual products. Wise company takes concrete steps to manage successful relations with its key publics.
The PR department in most companies monitor attitudes of the organizations' public and distributes information & communication to build goodwill.

Public relations are often under-used by marketers, yet a well-thought out program coordinated with the other promotion-mix elements can be extremely effective.
The appeal of public relations and publicity is based on three distinctive qualities:

- High credibility
- Ability to catch buyers of guard
- Dramatization

Marketing public relations (MPR) support corporate or product promotion and image-making.
MPR plays an important role in the following tasks:

- Assisting in the launch of new products
- Assisting in repositioning a mature product
- Building interest in a product category
- Influencing specific target groups
- Defending product that have encountered public problems, and
- Building the corporate image in a way that reflects favorably on its products.

Corporate Affairs

- A collection of strategic activities aimed at marketing an organization, its issues, and its ideals to potential stakeholders (consumers, general public, shareholders, media, government, and so on).

Goal of Public Relations

- To track public attitudes, identify issues that may elicit public concern, and develop programs to create and maintain positive relationships between a firm and its stakeholders

Use of Public Relations

- To promote the firm, its people, its ideas, and its image
- To create an internal shared understanding among employees

Public Relations Methods

- News/press releases
- Feature articles
- White papers
- Press conferences
- Event sponsorship
- Product placement
- Employee relations

3. **Events & Experiences (Sponsorship)**

Marketers report a number of reasons why they sponsor events:

- To identify a particular target market of lifestyle.
- To increase awareness of company or product name.
- To create or reinforce consumer perceptions of key brand image associations.
- To enhance corporate image dimensions.
- To create experience & evoke feelings.
- To express commitment to the community or on social issues
- To permit merchandising or promotional opportunities.

The marketing objectives and communication strategy that must be met by the event are:

- The audience delivered by the event must match the target market of the brand.
- The event must have sufficient awareness.
- The event must possess the desired image.
- The event must be capable of creating the desired effect with that target market.
- Consumers must make favorable attributions to the sponsors for the event.

An ideal event might be the one that:

- The audience closely matches the desired target market
- Generates much favorable attention
- Is unique but not encumbered with many sponsors
- Lends itself to ancillary marketing activities
- Reflects of enhances the brand or corporate image of the sponsor.

More and more firms are also using their names to sponsor the arenas, stadiums and other venues that actually hold the event.

Designing Sponsorship Programs

- The event itself does not guarantee sponsorship success but it is the marketing program accompanying an event sponsored that determines the sponsorship success.
- Companies should spend at least two to three times the amount of the sponsorship expenditure or related marketing activities.
- For non-profit organizations, event creation is very important in publicizing fund-raising event.

Measuring sponsorship activities

- As with public relations, measurement of the success of sponsorship events is difficult.
- Two basic approaches in measuring the effects of sponsorship activities:
  - **Supply side method** focuses on potential exposure to the brand by accessing the extent of media coverage.
  - **Demand side method** focuses on reported exposure from consumers.
- **Supply side methods** attempt to approximate the amount of time or space devoted to media coverage of an event.
  - This measure was then translated into an equivalent 'value' according to the fees associated in actually advertising product in the particular media vehicle.

- However, validity of this method can be questioned:
  - In equating media, coverage with advertising product's content is ignored.
  - Even though advertisers fully use media space and time to communicate a strategically designed message, media coverage and telecasts only expose the brand, and do not necessarily embellish its meaning in any direct way.

– **The demand side method** attempts to identify the effects sponsorship has on consumers' brand knowledge. Tracking or customized surveys can explore the ability of the events sponsors they want to effect by:
  - Awareness,
  - Attitudes, and
  - Sales.

4. **Personal Selling and Sales Management**
   - Focused less on "sales" and more on developing long-term, personal relationships with buyers
   - The most precise form of communication, but with very high cost per contact
   - Has evolved to take on elements of customer service and marketing research
   - The frontline knowledge held by the sales force is one of the most important assets of the firm.
   - It occurs when a salesperson sells a product, service, or solutions to client.
   - Salespersons normally match the benefits of their offering to the specific needs of a client.
   - Personal selling is the most effective tool at later stages of the buying process, particularly in building up buyer preference, conviction, and action.

   Personal selling has three distinctive qualities:
   - Personal interaction
   - Cultivation, and
   - Response

   The Sales Management Process:
   - Developing sales force objectives
   - Determining sales force size
   - Recruiting and training salespeople
   - Controlling and evaluating the sales force

   The Impact of Technology on Personal Selling
   - Integrated supply chains and e-procurement have reduced the size of the sales force.
   - How can firms use new technology to reduce costs and increase productivity while maintaining personalized, one-to-one client relationships?

5. **Sales Promotion**
   - Accounts for the bulk of promotional spending in many firms
   - Activities that create buyer incentives to purchase a product or that add value for the buyer or the trade
   - Has one universal goal: to induce product trial and purchase
   - Typically used to support other promotional activities rather than as a stand-alone promotional element
   - Companies use sales-promotion tools to draw a stronger and quicker buyer response.

   Sales promotion can be used for short-run effects. Sales promotion offer three distinct benefits:
   - Communication
   - Incentive
   - Invitation

   Sales Promotion in Consumer Markets:
   - Coupons
   - Rebates
   - Samples
   - Loyalty programs
   - Point-of-purchase
   - Premiums
   - Contests and sweepstakes
   - Direct mail

   Sales Promotion in Business Markets:
   - Trade allowances
   - Free merchandise
   - Training assistance
   - Cooperative advertising
   - Selling incentives

6. **Direct and Interactive Marketing**
   - There are three main forms of direct marketing: direct mail, telemarketing, and Internet marketing.
   - Interactive marketing is the newest channel that allows marketers to communicate with the target audience via electronic medium and the Internet.
   - Both direct & interactive marketing share three distinctive characteristics. They are:
     a. Customized
     b. Up-to-date
     c. Interactive

7. **Word-of-mouth Marketing**
   - Word-of-mouth also takes many forms online or offline. Online can be social media, social networking and viral marketing.
   - Three noteworthy characteristics are:
     a. Influential

b. Personal, and
c. Timely

- Positive word-of-mouth can be sometimes considered a part of advertising, where it is effective for smaller businesses, with whom customers may feel a more personal relationship.

POINTS TO PONDER

1. Modern marketing calls for more than developing a good product, pricing it attractively, and making it accessible to target customers. Companies must also communicate with present and potential stakeholders and with the general public.
2. The marketing communications mix consists of eight major modes of communication: advertising, sales promotion, public relations and publicity, events and experiences, direct marketing, interactive marketing, word-of-mouth marketing, and personal selling.

SELF-CHECK

1. Review the steps in the AIDA model. In what ways has promotion affected you in various stages of this model? Does promotion affect you differently based on the type of product in question? Does the price of the product (low versus high) make a difference in how promotion can affect your choices? Explain.
2. What does the future hold for traditional mass-media advertising? If you were the CEO of a major television network, magazine publisher, or newspaper company, what you be doing now to ensure the livelihood of your company in 10 to 20 years?
3. What would happen if a company suddenly stopped using sales promotion activities after having used them for a long period of time? Is it possible for a company to become dependent on the use of sales promotion activities? Explain.

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